Petition

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No. 81-

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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QUESTION PRESENTED FOR REVIEW

Whether the Court below properly reversed the determination of the Federal Energy Regulatory Commission that pipeline production which becomes part of its general gas supply along with natural gas purchased from producers or other pipelines for ultimate resale to the pipelines' customers and which had been priced in the pipelines' cost-of-service on a cost basis does not involve a "first sale" of natural gas, as that term is defined in the Natural Gas Policy Act of 1978, entitled to secure the maximum lawful ceiling prices prescribed by Title I of that Act of 1978.

PARTIES BELOW

American Gas Association
Arizona Electric Power Cooperative and City of Wilcox
Ciba-Geigy Corporation
Colorado Interstate Gas Company
Columbia Gas Transmission Corp.
Consolidated Gas Supply Corp.
Ecee, !nc.
El Paso Natural Gas Company
The Federal Energy Regulatory Commission
Kansas-Nebraska Natural Gas Company
Kansas State Corporation Commission
Kentucky-West Virginia Natural Gas Company
Michigan-Wisconsin Pipe Line Company
Mid Louisiana Gas Company
Natural Gas Pipeline Co. of America
Northern Natural Gas Company
Northwest Pipeline Corp.
The Public Service Commission of the State of New York
The Public Service Commission of Wisconsin
The State of Michigan and The Public Service Commission of Michigan
Southern Natural Gas Company
United Gas Pipe Line Corp.

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

PARTIES BELOW ii

TABLE OF AUTHORITIES iv

OPINIONS AND ORDERS BELOW 2

JURISDICTION 2

STATUTES INVOLVED 3

STATEMENT OF THE CASE 3

1. *The Regulatory Background* 4

2. *The Natural Gas Policy Act of 1978* ... 6

3. *The Proceedings Below* 8

REASONS FOR GRANTING THE WRIT 10

CONCLUSION 20

APPENDIX

TABLE OF AUTHORITIES

Judicial Decisions: **Page**

Columbia Gas Development Corp. v. FERC, 651 F.2d 1146 (5th Cir. 1981) 11

Commissioner of Internal Revenue v. Freihofer, 102 F.2d 787 (3rd Cir. 1939) 17

Lee, Inc. v. FERC, 611 F.2d 554 (5th Cir. 1980) 11

Helvering v. Nebraska Bridge Supply & Lumber Co., 115 F.2d 288 (8th Cir. 1940) 17

Pennzoil Company v. FERC, 645 F.2d 360 (5th Cir. 1981) *cert. denied*, 102 S. Ct. 1000 (1962) 15

Phillips Petroleum Company v. Wisconsin, 347 U.S. 672 (1954) 4

Posados v. Natinal City Bank, 296 U.S. 497 (1936) 12

United States v. United Continental Tuna, 425 U.S. 164 (1976) 12

Administrative Decisions:

Canadian River Gas Co., 3 F.P.C. 32 (1942), *aff'd sub nom., Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581 (1945) 4

Just and Reasonable National Rates for Sales of Natural Gas, 52 F.P.C. 1604 (1974), *aff'd, Shell Oil Company v. F.P.C.*, 520 F.2d 1061 (5th Cir. 1976), *cert. denied*, 426 U.S. 941 (1976) 6

National Rates for Jurisdictional Sales of Natural Gas, 56 F.P.C. 509 (1976) *aff'd sub nom., American Public Gas Ass'n. v. FPC*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978) 5

Permian Basin Area Rate Proceeding, 34 F.P.C. 159 (1965) *aff'd, Permian Basin Area Rate Cases*, 390 U.S. 747 (1968) 4, 5

Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738 (1969), *aff'd, City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972) 5

Pricing of Pipeline Production Under the Natural Gas Act, Docket No. RM80-6, Notice of Proposed Rulemaking, 44 *Fed. Reg.* 66612 (November 20, 1979) 8, 9

Statutes:

Natural Gas Act, 15 U.S.C. §§717a, *et seq.* 2

Natural Gas Policy Act of 1978, 15 U.S.C. §§3301, *et seq.* ..... *passim*

Section 2(20), 15 U.S.C. §3301(20) 16
Section 2(21), 15 U.S.C. §3301 (21) ..... *passim*
Section 101(b) (9), 15 U.S.C. §3311 (b)(9) 7, 15
Section 108, 15 U.S.C. §3318 19
Section 203(b)(1), 15 U.S.C. §3343(b)(1) 16
Section 203(b) (2), 15 U.S.C. §3343(b) (2) ... 15, 16
Section 501, 15 U.S.C. §3411 12
Section 506, 15 U.S.C. §3416 ..... 3, 9
Section 601(b)(1)(E), 15 U.S.C. §3431(b)(1)(E) 15
Section 601(c), 15 U.S.C. §3431(c) 15
Section 602, 15 U.S.C. §3432 14

Fifth Circuit Court of Appeals Reorganization Act of 1980, Pub. L. 96-452, 94 Stat. 1994 (October 14, 1980) 2

Miscellaneous:

Statistics of Interstate Natural Gas Pipeline Companies - 1979, U.S. Department of Energy, issued October 1980 17

H.R. 1758, 81st Cong. 2nd Sess., vetoed April 15, 1950, H.R. Doc. No. 555, 81st Cong. 6

H.R. 6645, 84th Cong. 2nd Sess., vetoed February 17, 1956, H.R. Doc. No. 342, 84th Cong. 2nd Sess. 6

S. Rep. No. 95-1126, 95th Cong., 2nd Sess. (1978) 7

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MID LOUISIANA GAS COMPANY, *et. al.*,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The Public Service Commission of the State of New York ("New York"), an intervenor-respondent in the court below, petitions for a writ of certiorari to review the December 23, 1981 decision of the United States Court of Appeals for the Fifth Circuit in *Mid Louisiana Gas Company, et al.*, v. *Federal Energy Regulatory Commission*, Case No. 80-3804, and *Consolidated Gas Supply Corporation* v. *Federal Energy Regulatory*

Commission, Case No. 80-4010.[1] The Court's decision vacated Order Nos. 58 and 98 issued by the Federal Energy Regulatory Commission ("Commission" or "FERC") on November 14, 1979, and August 4, 1980, respectively, (as reaffirmed on rehearing by Order No. 102, issued on October 3, 1980), relating to the pricing of pipeline produced gas under the Natural Gas Policy Act of 1978, 15 U.S.C. §§3301, *et seq.*, and the Natural Gas Act, 15 U.S.C. §§717a, *et seq.*.

OPINIONS AND ORDERS BELOW

The opinion of the United States Court of Appeals for the Fifth Circuit is reported at 664 F.2d 530, and is reprinted in Appendix A. The Commission's Order Nos. 58, 98 and 102 are not reported and are set out in Appendix B.[2]

JURISDICTION

The judgment of the United States Court of Appeals for the Fifth Circuit was entered on December 23, 1981 (App. C-1). On January 11, 1982 the Court extended the time for petitions for rehearing until January 20, 1982 (App. C-2). Petitions for rehearing filed by New York, the State of Michigan and the Arizona Electric Power Cooperative, Inc. were denied on February 5, 1982 (App. C-3). This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

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[1]The case below was heard and decided before the effective date of the Fifth Circuit Court of Appeals Reorganization Act of 1980, Pub. L. 96-452, 94 Stat. 1994 (October 14, 1980). Since the first of the several petitions for review of the FERC orders was filed by Mid-Louisiana Gas Company, which resides, is located and has its principal place of business in the present Fifth Circuit, it would appear that that circuit would retain jurisdiction in the event of a remand by this Court. See NGPA Section 506, 15 U.S.C. §3416; 28 U.S.C. §2112.

[2]Reference to the Appendix to this petition are hereafter given as "(App. ___)".

STATUTES INVOLVED

The Statute upon which the court of appeal's decision is based is the Natural Gas Policy Act of 1978, 15 U.S.C. §§3301, *et seq.*, the relevant portions of which appear in Appendix D.

STATEMENT OF THE CASE

Title I of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. §§3301 *et seq.*, provides for various categories of "maximum lawful ceiling prices" applicable to "first sales" of natural gas as that term is defined in Section 2(21) of the Act. 15 U.S.C. §3301(21) (App. D-1). The Federal Energy Regulatory Commission which is authorized by Section 501 of the Act, 15 U.S.C. §3411, (App. D-3) to administer and interpret the Act, concluded in Order No. 58 (App B-1) that the only sales "attributable" to a pipeline's production, and thus qualifying as a first sale, were sales of the pipeline's production from discrete wells to specific customers; the larger percentage of pipeline production which is, instead, commingled with the gas purchased by the pipeline from independent and affiliated producers for resale to its customers, did not, the Commission concluded, involve a first sale and remained subject to the Commission's jurisdiction under the Natural Gas Act. The court below, holding that no great deference was due to the Commission's construction, reached the opposite conclusion.[3] In its view the legislative history of the NGPA showed a clear Congressional intent that the intracorporate transaction by which gas was transferred from the production "division" of the pipeline to its transportation "division" be construed as a "transfer for value" constituting a "first sale" of the gas

[3]The basis for the jurisdiction of the United States Court of Appeals for the Former Fifth Circuit is Section 506 of the Natural Gas Policy Act of 1978, 15 U.S.C. §3416.

within the meaning of Section 2(21). The Commission, accordingly, was required to permit pipelines to secure the appropriate maximum lawful ceiling rates for *all* of their gas production.

1. The Regulatory Background

Regulation of pipeline production operations under the Natural Gas Act followed quite a different course than that of independent producers. Prior to this Court's opinion in *Phillips Petroleum Company* v. *Wisconsin*, 347 U.S. 672 (1954), the Commission believed it had no jurisdiction over the rates for sales of natural gas *to* a pipeline. However, from the inception of regulation under the Natural Gas Act in 1938, the costs incurred *by* pipelines in producing their own gas had been included in the cost-of-service upon which their rates to their customers were based. *Canadian River Gas Co., et al.*, 3 F.P.C. 32 (1942), *aff'd sub nom., Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945). This did not take the form of determining a "just and reasonable" price for each unit of gas produced; rather all of the pipeline's prudent production costs were either capitalized or expensed regardless of the success or failure of their efforts. This methodology essentially removed the risk of failure from the pipelines' production operations since they earned a fair return on all prudent production investments regardless of the success of the ventures.

The regulation of the prices at which independent producers sold gas to the pipelines which emerged after *Phillips, supra*, followed a different regulatory path. Under the "area" and subsequent "nationwide" approach, as initially established in the *Permian Basin Area Rate Proceeding*, 34 F.P.C. 159 (1965), *aff'd, Permian Basin Area Rate Cases*, 390 U.S. 747 (1968), and carried over with some modifications in subsequent

producer proceedings, a two price system was adopted establishing ceiling rates for each Mcf of flowing or new gas sold, with the flowing gas rates based primarily upon average industry historical costs and the higher new gas rates reflecting the average current cost of developing and producing gas. *Permian Basin Area Rate Cases, id; National Rates for Jurisdictional Sales of Natural Gas*, 56 F.P.C. 509 (1976), *aff'd sub nom., American Public Gas Ass'n. v. FPC*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978). Unlike cost-of-service pricing, the area or national rates were unit rates applied to each Mcf of gas sold. This methodology placed the risk of failure upon the producer.

In 1964 the Commission instituted a proceeding to determine whether it was reasonable within the governing standards of the Natural Gas Act to modify its established cost-of-service methodology for pricing pipeline production in the light of the on-going area rate proceedings involving producer sales to pipelines. In *Pipeline Production Area Proceeding (Phase I)*, 42 F.P.C. 738, 1089 (1969), *aff'd, City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971) *cert. denied*, 405 U.S. 1074 (1972), the Commission concluded that with respect to pipeline production *from leases acquired after the date of its determination* (October 8, 1969), the public interest in encouraging pipeline production would be served by pricing such gas at the appropriate rate applicable to sales of gas by independent producers. It also made clear that it would apply the area rate to pipeline production sold "off-system" at the wellhead to other pipelines. 42 F.P.C. at 746. However, this holding was not made applicable to pipeline production from the pre-October 8, 1969 leases. Production from such leases continued to be priced on

a cost-of-service basis.[4]. In addition, certain pipelines decided to forego collection of area or national rates and, at their request, were authorized by the Commission to price some of their production from newer wells or leases on a cost-of-service basis.

2. The Natural Gas Policy Act of 1978

The issue of the extent to which the prices under which producers of natural gas sell their gas to the interstate pipeline should be subject to federal regulation has been a matter of controversy ever since *Phillips, supra.* Twice in the 1950's Congress passed legislation eliminating such regulation, but in both cases the bills were the subject of Presidential veto. In each case the issue of pipeline production was expressly addressed. The 1950 bill[5] excluded pipeline production from the proposed deregulation. The 1956 bill[6] contained a separate provision (as a new Section 5(f) of the Natural Gas Act) specifying that in rate proceedings the pipeline would be allowed the reasonable market price of any gas produced by it as an operating expense.

Legislation to modify the nature of producer regulation became a live issue again in the mid-1970's in the light of curtailment of pipeline service stemming from inadequate interstate gas supplies coupled with

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[4]The one exception is that in 1974 the Commission concluded that pipeline production on old leases from wells commenced after January 1, 1973 would secure the nationwide rate. *Just and Reasonable National Rates for Sales of Natural Gas,* 52 F.P.C. 1604, 1656, (1974), *aff'd, Shell Oil Company* v. *FPC,* 520 F.2d 1061 (5th Cir. 1976), *cert. denied,* 426 U.S. 941.

[5]H.R. 1758, 81st Cong., 2nd Sess., vetoed April 15, 1950, H.R. Doc. No. 555, 81st Cong., 2nd Session.

[6]H.R. 6645, 84th Cong., 2nd Sess, vetoed February 17, 1956, H.R. Doc. No. 342, 84th Cong., 2nd Sess.

the general energy crisis resulting from the rapid increase in oil prices caused by the formation of OPEC. Various and conflicting proposals were advanced ranging from complete deregulation to imposition of federal control over sales in the intrastate market exempted from regulation under the Natural Gas Act. However, throughout the more than two year period in which the compromise legislation which became the NGPA was before the Congress, no sponsor of legislation expressed any dissatisfaction with the existing regulation of pipeline production or suggested that the cost-of-service treatment of some of this production was operating in a manner contrary to the public interest and should be eliminated.

The legislation that emerged as the NGPA provided in Title I for a series of "maximum lawful ceiling rates" for various categories of "first sales" of natural gas, with some categories to be deregulated at specified dates and others to remain subject to regulation. Pursuant to the provisions of Section 101(b)(9), 15 U.S.C. §3311(b)(9), these rates were to be available only to the extent they did not exceed the contract price for the first sale. The term "first sale" was defined in Section 2(21) as the sale of any volume of gas *to* an interstate or intrastate pipeline, local distribution company or end user but as not including any sale *by* an interstate or intrastate pipeline, local distribution company or affiliate thereof "unless such sale is attributable to volumes of natural gas produced" by such an entity. Neither the Conference Report on the bill[7] nor any other statement in the legislative history provides any further elucidation of this language.

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[7]S. Rep. No. 95-1126, 95th Cong., 2nd Sess., August 18, 1978.

3. The Proceedings Below

The NGPA became law on November 9, 1978. On November 28, 1978, the FERC issued Interim Regulations governing the operation of Title I of the Act.[8] Section 270.203(a) of these regulations, 43 *Fed. Reg.* 56549-50, provided that a sale of gas by a pipeline was only "attributable" to the pipeline's own production within the meaning of Section 2(21)(B) of the Act when the sale was exclusively of volumes from identifiable wells, properties or reservoirs owned by the pipeline, such as the off-system wellhead sales of pipeline produced gas which had traditionally been treated by the Commission as if they were sales by an independent producer.

On November 14, 1979, the Commission issued its Order No. 58 in Docket No. RM80-7, which prescribed its "Final Rule Governing the Maximum Lawful Price for Pipeline, Distributor or Affiliate Production" under the NGPA (App. B-1). With respect to pipeline production the Commission, rejecting the contrary contentions by a number of pipelines, essentially reaffirmed its determination in the Interim Regulations.[9] Since the Commission recognized that this action would leave most pipeline production subject to its regulatory authority under the Natural Gas Act, it simultaneously issued a Notice of Proposed Rulemking in Docket No. RM80-6 to consider the extent to which in the exercise of this authority it should price pipeline production at

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[8]43 *Fed. Reg.* 56448, *et seq.* (December 1, 1978)

[9]Contrary to the provisions of Section 270.203(a) of the Interim Regulations, Order No. 58 concluded that all sales by pipeline affiliates, including those to the pipeline itself, were attributable to the affiliates' production and eligible for Title I ceiling rates if the sales contract authorized their collection.

NGPA levels or adhere to existing procedures and standards for pricing such gas.[10]

On August 4, 1980, the Commission issued Order No. 98, in Docket No. RM80-6, its "Final Rule Governing Pricing of Pipeline Production Under the Natural Gas Act" (App. B-14). This Order amended the Commission's Regulations under the Natural Gas Act and added a new Section 154.42, 18 C.F.R. §154.42. The new rule had the effect of pricing all pipeline company-owned and affiliate production (not already qualifying for NGPA first sale treatment under Order No. 58) at the applicable NGPA ceiling rates for independent producer sales of similar gas unless such gas was currently being priced on a cost-of-service basis. This latter category of gas, for which gas consumers had already paid most of the pipeline's costs, was maintained on a cost of service basis.

Petitions for rehearing of Order Nos. 58 and 98 were filed by a number of parties, and on October 3, 1980, the Commission issued Order No. 102 which, except for a minor clarification of Order No. 98 not here material, denied rehearing of both Order No. 58 and Order No. 98 (App.B-50).

Separate appeals were then taken by a number of pipelines pursuant to Section 506(b) of the NGPA, 15 U.S.C. § 3416(b), both from Order No. 58 as reaffirmed by Order No. 102 (consolidated in the 5th Circuit[11] under the style *Mid-Louisiana Gas Company, et al.* v.

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[10]*Pricing of Pipeline Production Under the Natural Gas Act*, Docket No. RM80-6, Notice of Proposed Rulemaking, 44 *Fed. Reg.* 66612 (November 20, 1979).

[11]Petitions for review of both Order Nos. 58 and 98 were filed in a number of circuits but all were eventually transferred to the 5th Circuit.

FERC, No. 80-3804) and from Order No. 98 as reaffirmed by Order No. 102 (consoldiated below under the style *(Consolidated Gas Supply Corporation, et al.* v. *FERC*, No. 80-4010). New York intervened in support of the Commission. The two sets of cases were argued together and on December 23, 1981, the Court issued its opinion holding that all pipeline production constituted a first sale within the meaning of Section 2(21) and vacating both Order Nos. 58 and 98.[12] On timely motions, the court, by order of January 11, 1982, extended the time to file applications for rehearing until January 20, 1982. A timely application for rehearing was filed by New York, and suggestions for rehearing *en banc* by the State of Michigan and the Arizona Electric Power Corporation. By order of February 5, 1982, the applications for rehearing or rehearing *en banc*, were denied (App. C-3).

REASONS FOR GRANTING THE WRIT

This case presents an important question of first impression: whether the Natural Gas Policy Act of 1978 in establishing a series of maximum lawful ceiling prices for the "first sales" of natural gas, repealed the Commission's regulatory authority under the Natural Gas Act over all production operations of

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[12]The Court opinion vacates Commission Order No. 98 without reaching the issues raised in Case No. 80-4010 (other than an issue as to special relief it found not ripe for review) "becuase we hold that the Commission lacked authority to set prices for interstate pipeline production under the NGA" (App. A-15). In the event his Court were to find that the court of appeals erred in setting aside Order No. 58 it would be required as well to set aside its vacation of Order No. 98 and to remand the case to the court of appeals for consideration of the challenges to Order No. 98 on their merits.

interstate pipelines. Section 2(21)(B) of the NGPA, 15 U.S.C. §3301(21)(B), excludes from the first sales entitled to secure the maximum lawful ceiling prices established by Title I of the Act "the sale of any volume of natural gas by an interstate pipeline...unless such sale is attributable to volumes of natural gas produced by such interstate pipeline." The Commission held that pipeline production would involve a first sale under this definition only where the pipeline makes discrete sales of its own production directly to other pipelines, distributors or end users and does not comprehend the major portion of a pipeline's gas production which, along with gas purchased from producers or other pipelines, becomes part of the pipeline's system gas supply for subsequent resale to its customers. The court below concluded, however, that Congress intended the intracorporate transaction by which gas is transferred from the pipeline's production "division" to its transportation "division" to be treated as a "transfer for value" constituting a "first sale" within the meaning of Seciton 2(21). This holding, which makes *all* pipeline production eligible for the NGPA ceiling rates, and increases the cost of gas to consumers by hundreds of millions of dollars per year, is wrong as a matter of statutory construction, fails to afford proper deference to the contemporaneous interpretation of a statute by the agency empowered to administer it,[13] and results in

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[13]The Court of Appeals concluded that it was not required to give the Commission's construction of the NGPA here the degree of deference it had afforded Commission rules interpreting other provisions of the same statute (see *Columbia Gas Development Corp.* v. *FERC*, 651 F.2d 1146, 1155 (5th Cir. 1981); *Ecee, Inc.* v. *FERC*, 611 F.2d 554, 563 (5th Cir. 1980)) because the Commission's construction, though contemporaneous, had not received the sanction of long years of application and tacit Congressional approval, and because the court believed the Commission had no

the improper repeal by implication of forty years of commission regulation of pipeline production under the Natural Gas Act.

1. The decision below holds that the Commission was required to find that intracorporate transfers of gas constitute a "transfer of value" and hence a "first sale" within the meaning of Section 2(21) of the NGPA, because nothing in the language of the Act "suggests any intent to deny NGPA pricing to natural gas just because it is produced by a pipeline" (App. A-8). The court's suggestion that the established Commission regulation of pipeline production under the Natural Gas Act is to be repealed unless legislation intended to modify producer regulation manifests an intent not to cover pipeline production as well, is in direct conflict with the established maximum of statutory construction that repeal by implication is not favored. See *Posades* v. *National City Bank*, 296 U.S. 497, 503 (1936); *United States* v. *United Continental Tuna*, 425 U.S. 164, 168 (1976).

The pricing provisions of Title I of the NGPA were intended to correct what Congress perceived as deficiencies in the regulation of producer sales of natural gas in interstate commerce under the Natural Gas Act. One of the most distinctive features of the legislation is the complete absence of any discussion in the legislative reports or debates of the existing regulation of pipeline production under the Natural Gas Act, and particularly of the established Commission policy to price gas from older leases on a cost-of-service basis, and to maintain such regulatory treatment once a

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special expertise in defining the meaning of the term "first sale." Neither of these reasons justify the court's *de novo* construction of an Act which the Commission was expressly authorized to administer and construe. See NGPA Section 501, U.S.C. § 3411 (App. D-3)

pipeline had received the benefits of cost-of-service treatment for new gas production. Nothing in the NGPA specifies that the Commission's authority over all pipeline production under the Natural Gas Act is to be superseded by the rate structure adopted for producers, who, unlike pipelines, had never been regulated on an individual company cost-of-service basis permitting recovery of the full costs of production operations regardless of the amount of gas produced.

2. The decision below purports to surmount these difficulties by concluding that: A) while Congress did not direct itself to pipeline production, its objective "to eliminate the dual interstate and intrastate market for natural gas and to provide the higher prices to encourage production" cannot be served by "creating" a distinction between pipeline and independent producers (App. A-9); B) since the last clause of Section 2(21) contemplates that *some* pipeline production may qualify as first sales, it can only have meaning if it is interpreted in a manner which will characterize *all* pipeline production as first sales (App. A-8); and C) the legislative history of the Act indicates Congress intended to accord all pipeline production first sale status (App. A-11). None of these three predicates for the court of appeals' holding are supportable.

A. There is no suggestion throughout the lengthy legislative history of the NGPA that Congress believed that the existing state authority over the production efforts of intrastate pipelines and distributors to augment their system gas supply sold within the state was a significant element of the dual market problem which had arisen under the Natural Gas Act under which gas producers sold gas in interstate commerce at regulated prices and in the intrastate market on an

unregulated basis. While the NGPA for the first time imposes regulation upon sales by producers to intrastate customers there is nothing whatsoever to indicate that it was intended to preempt the existing state regulation over the cost of gas produced by intrastate pipelines or distributors for sale to their customers, or to preclude state regulatory agencies from pricing such gas on a cost-of-service basis. On the contrary, Section 602(a) of the Act, 15 U.S.C. §33432(a) (App. D-4) expressly preserves the states' authority to prescribe maximum rates lower than those authorized in Title I of the Act for first sales of natural gas. Nor is there any support for the suggestion that Congress believed that maintenance of the situation under which the old flowing gas production of interstate pipelines was priced on a cost-of-service basis would in any way limit optimum gas production. Unlike the case of independent producer price regulation under the Natural Gas Act, all increased costs of such pipeline production, including those resulting from inflation and decreasing levels of production from old wells, would be reflected in increases in the pipeline's cost of service and thus recovered by the pipeline.

B. The court of appeals' conclusion that it was necessary to treat intracorporate transfers as first sales to give any meaning to the final clause of Section 21(21)(B) of the NGPA is clearly incorrect. The clause specifies that pipeline sales will not be treated as first sales "unless such sale is attributable to volumes of natural gas produced by such interstate pipeline". The Commission's interpretation of the clause as applicable only to pipeline contracts for the well head or off-system sales of discrete volumes of their produciton, which under the Natural Gas Act were treated like sales

by independent producers, does not make the "unless" clause meaningless because most pipeline production is not sold in this manner but, instead, becomes part of the pipeline's overall gas supply for subsequent resale. The court's construction, on the other hand, produces the bizzare result that pipeline production which is not the subject of any sales contract is automatically entitled to the maximum ceiling rates of Title I of the NGPA, while the producers' rates remain limited by the terms of their sales contracts. See NGPA Section 101(b)(9), 15 U.S.C. §3311(b)(9) (App. D-2), *Pennzoil Corporation* v. *FERC*, 645 F.2d 360 (5th Cir. 1981), *cert. denied*, 102 S. Ct. 1000 (1982).[14]

C. The Court of Appeals purported to find support for its conclusion that Congress "both intended to accord pipeline production first sale status and contemplated that the intracorporate transfer would be treated as a first sale" in Section 203(b)(2) of the NGPA, 15 U.S.C. § 3343(b)(2) (App. D-2), which specifies that "the first sale acquisition cost" of pipeline production under the incremental pricing provisions of Title II of the Act, "shall be determined in accordance with rules prescribed by the Commission", and in language in the Conference Report on the NGPA stating that the Commission "may define terms such as

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[14]It should also be noted that Section 601(b)(1)(E) of the NGPA, 15 U.S.C. § 3431(b)(1)(E), provides that a pipeline's purchase of gas from an affiliate will only be deemed to be "just and reasonable", and subject to the terms of the "pass-through" provisions of Section 601(c), if the price provided under the sales contract is consistent with the prices of the pipeline's purchases from independent producers. No such statutory protection is afforded with respect to pipeline production taken into the pipeline's system supply without any sales contract. It is inconveivable that equivalent protection to gas consumers would not have been provided with respect to pipeline production if the Congress had contemplated that all such production would qualify as a first sale.

'transfer for value' used in the definition of first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition".[15] Neither of these provisions supports the court's conclusion.

The Commission was authorized to determine the "first sale acquisition cost" of pipeline production by Section 203(b)(2) because Title II of the Act provided for passthrough to specified categories of customers of the difference between the "first sale acquisition cost" of various categories of gas and various "incremental pricing thresholds" and Congress was aware that pipeline production becoming a part of the pipeline's general gas supply had no fixed acquisition cost. If Congress had assumed that all pipeline production would be treated as a first sale falling within one of the Title I pricing categories there would be no need for the exception to the "general rule" of Section 203(b)(1). Moreover, if Congress had contemplated that the "first sale acquisition cost" attributed to pipeline production for the special purposes of Title II, would necessarily be the "maximum ceiling prices" authorized under Title I, it could have said so rather than providing that the cost was "to be determined by the Commission."

The Conference Report reference to the power of the Commission to define the term "transfer for value", used in the definition of a "sale" in Section 2(20) of the Act,[16] and to prescribe rules applicable to intracorporate transactions, cannot properly be characterized as requiring the Commission to find the physical transfer of gas from the production to the transportation "division" of a pipeline to be a

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[15]S. Rep. No. 95-1126, 95th Cong., 2d Sess., 116 (1978).

[16]Section 2(20) of the NGPA, 15 U.S.C. § 3301(20), provides that "the term 'sale' means any sale, exchange or other transfer for value" (App. D-1).

"transfer for value" qualifying as a "first sale." A "transfer for value" under the law of sales exists only where there is a transfer of title to property for consideration;[17] in the situation postulated by the court there is no transfer of title, no passage of consideration and no contract of agreement between separate parties. Nor is there anything in the Conference Report or elsewhere in the legislative history which indicates that Congress intended to require the Commission to exercise its discretionary authority to define terms in a manner contrary to their normal meaning.

3. The question of the proper treatment of pipeline production under the NGPA is an important one; while the annual cost to gas consumers if the decision below is permitted to stand is not presently susceptable to quantification, it is certain to be in the hundreds of millions of dollars, with little or no return by way of increased gas supplies. As of 1979 there were 26 Class A and B pipelines subject to the jurisdiction of the FERC which had production operations of their own, with total production during that year of 731,981,654 Mcf. See, *Statistics of Interstate Natural Gas Pipeline Companies-1979*, U.S. Department of Energy, issued October 1980, p. 221. Not all of this gas was priced upon a cost-of-service basis under the Commission's orders vacated by the court of appeals. As indicated, *supra* p. 9, cost-of-service treatment is limited under Order No. 98 (as it was prior to enactment of the NGPA) to gas from wells commenced prior to 1973 on leases acquired prior

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[17] "Where a transfer of property takes place without the transferor's receiving anything of value for the property transferred, the transfer is not a sale or exchange." *Helvering* v. *Nebraska Bridge Supply & Lumber Co.* 115 F.2d 288, 290 (8th Cir. 1940). See *Commission of Internal Revenue* v. *Freihofer*, 102 F.2d 787, 789 (3rd Cir. 1939).

to October 8, 1969, plus some newer pipeline production where the pipeline had been specially authorized to secure cost-of-service treatment. But the percentage of pipeline production which remains on a cost-of-service basis under the Commission's orders is clearly substantial. Thus, Columbia Gas Transmission Corporation, a pipeline serving New York, has introduced evidence in a pending case that 76.43% of its production for the year ending February 28, 1982, or 30,835,900 Mcf out of a total production of 40,268,900 Mcf, was priced on a cost-of-service basis. See Exhibit 52 in *Columbia Gas Transmission Corp.*, Docket No. TA81-1-29, *et al.* Similarly, Consolidated Gas Supply Corporation, another major pipeline serving New York, in Schedule R of its rate filing in Docket No. RP80-61 stated that of its 37,524,193 dt of pipeline production for the year ending September 30, 1979, 26,726,751 dt, or 71.23% was old gas priced upon a cost-of-service basis.

Few of the affected pipelines have as yet stated their claims[18] and unresolved questions are presented as to how pipeline production for which there is no sales contract and which was never priced at a just and reasonable rate would be treated if the intracorporate

[18]El Paso Natural Gas Company on March 1, 1982 submitted a rate increase filing in FERC Docket No. TA82-2-33, which, *inter alia*, reflects an annual increase of approximately $152,000,000 assertedly reflecting the repricing of its produciton to reflect the *Mid-Louisiana* decision. Of this amount, $109 million was said to represent retroactive application of the decision to the effective date of the NGPA. Similarly, on March 29, 1982, Colorado Interstate Gas Company submitted a general rate increase filing in Docket No. RP82-54-000 which, *inter alia*, reflects a retroactive impact of $104,618,064, and a prospective annual increase of $22,948,093 resulting from the repricing of company-owned cost-of-service production at NGPA rates.

transactions are classified as "first sales". It seems clear, however, that a substantial and increasing percentage of the pipelines' cost-of-service production, particularly that from the pre-1973 wells on pre-1970 leases, will qualify for the "stripper well" price provided by Section 108 of the Act, 15 U.S.C. §3318, for gas from wells with an average daily production of 60 Mcf per day or less. This is among the highest priced regulated gas under Title I of the NGPA with a ceiling price as of April, 1982 of $3.314 per Mcf (exclusive of state severance taxes), far higher than the unit cost of production for most of the affected pipelines. Thus, if only one half of Columbia's 30,835,900 Mcf cost-of-service gas for the year ending February 28, 1982 qualified as stripper well gas,[19] at a price of $3.314 rather than the 82 cents cost at which it is presently priced, the total annual cost to Columbia's customers from repricing this gas alone would be $38,390,695. This figure is consistent with a Consolidated Gas Supply Corporation projection that the net impact of the *Mid-Louisiana* opinion on its 1981 production of gas presently priced on a cost-of-service basis would be an annual increase in its jurisdiction rates of $27,725,000.

The volume of gas subject to cost-of-service pricing under Commission Orders 58 and 98 will tend to decline as the older wells play out. But this reduction in affected volumes of gas will be offset to an appreciable extent by the increasing spread between the effective ceiling

[19]This percentage is by no means out of line with probability. The Columbia filing in Docket No. TA81-1-29, *et al.*, indicates that 35.5% of its newer production already secures the Section 108 stripper well ceiling rate. The percentage of Columbia's cost-of-service production from pre-1973 wells qualifying for stripper well treatment will almost certainly be substantially greater since, after an initial period of optimum production, gas wells normally operate at a steadily declining rate.

rates under the NGPA which escalate at an annual inflation rate, and the cost-of-service prices for flowing gas, where only the relatively small operating costs are subject to inflation. Moreover, the immediate impact upon gas consumers will be substantially multiplied if, as a number of the affected pipelines have already asserted, the decision below must be applied retroactively to the December 1978 effective date of the NGPA. See n.18, *supra*. In short, the massive windfall profits which will accrue to a singificant number of pipelines as a result of the opinion below - without requiring any new production effort or expense by the pipelines - militates strongly in favor of granting the writ to review the decision below.

CONCLUSION

The court of appeals determination that all pipeline production is entitled to receive the maximum lawful ceiling prices prescribed by the NGPA for first sales of natural gas presents serious legal questions of first impression which warrant plenary review by the Court. The multi-million dollar increase in annual costs for natural gas resulting from the reversal of the Commission's contrary construction of the Act emphasizes the importance of the case. Accordingly, the Public Service Commission of the State of New York urges the Court to grant the requested writ of certiorari.

Respectfully submitted,

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April 12 , 1982

Appendix

81-1889

No. 81-

Supreme Court, U.S.
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ALEXANDER L. STEVAS
CLERK

IN THE

Supreme Court of the United States

October Term, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et. al.*,

Respondents.

APPENDIX TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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TABLE OF CONTENTS

Page

Appendix A: Court Opinion
Mid-Louisiana Gas Co. et al. v. *FERC*, 664 F.2d 530 (5th Cir. 1981) A-1

Appendix B: Commission Orders

Order No. 58, Docket No. RM80-7 (Issued November 14, 1979) B-1

Order No. 98, Docket No. RM80-6 (Issued August 4, 1980) B-14

Order No. 102, Docket Nos. RM80-7 and RM80-6 (Issued October 3, 1980) B-50

Appendix C: Court Judgment and Orders on Rehearing

Mid Louisiana Gas Co. et al. v. *FERC*, Case No. 80-3804, Judgement of United States Court of Appeals for the Fifth Circuit C-1

Order Granting Extension of Time for Filing Petition for Rehearing C-2

Order Denying Petition for Rehearing and Suggestions for Rehearing En Banc C-3

Appendix D: Statues

Natural Gas Policy Act of 1978, 15 U.S.C. §§3301, *et seq.*
Section 2(20), 15 U.S.C. §3301(20) D-1
Section 2(21), 15 U.S.C. §3301(21) D-1
Section 101(b)(9), 15 U.S.C. §3311(b)(9) D-2
Section 203(b), 15 U.S.C. §3343(b) D-2
Section 501, 15 U.S.C. §3411 ..... D-3
Section 601(b)(1)(E), 15 U.S.C. §3431(b)(1)(E) .. D-4
Section 602, 15 U.S.C. §3432 ..... D-4

APPENDIX A

***Mid-Louisiana Gas Co.* v. *FERC*, 664 F.2d 530 (1981)**
***reh'g denied*, —— F.2d —— (5th Cir. 1982)**

APPENDIX A

664 F.2d 530

UNITED STATES COURT OF APPEALS,
FIFTH CIRCUIT.*

UNIT A

Dec. 23, 1981.

Nos. 80-3804, 80-4010.

MID-LOUISIANA GAS COMPANY, et al., *Petitioners,*

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

CONSOLIDATED GAS SUPPLY CORPORATION, et al.,
Petitioners,

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

Petitions for Review of Orders of the Federal Energy Commission. ⊥ 532

Before CLARK, Chief Judge, GARZA and SAM D. JOHNSON, Circuit Judges.

CLARK, Circuit Judge:

Petitioning pipeline producers of natural gas seek review of two issues concerning the scope and administration of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. § 3301 et seq. (Supp. III 1979). Their initial claim is that the Federal Energy Regulatory Commission (Commission)

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* Former Fifth Circuit case, Section 9(1) of Public Law 96-452—October 14, 1980.

incorrectly determined in Order No. 58 that the pricing structure established by the NGPA was not applicable to most gas produced by pipeline companies. Because we find this claim correct, we do not reach the producers' alternate claim that, if the Commission retained jurisdiction to establish the price of such gas, it abused its discretion in Order No. 98 by denying higher prices to gas which had previously been priced on a cost-of-service basis.

I.

Prior to the NGPA, the price for both the production and transportation of gas was regulated by the Commission under the Natural Gas Act of 1938 (NGA), 15 U.S.C. § 717 (1976). Under the NGA, the cost of gas which was brought by the pipelines for resale in interstate commerce was set according to area or national rates. Although the majority of gas transported by pipelines was bought from independent producers, some pipelines also produced their own gas, which was combined with gas bought from independent producers, and transported to their customers downline. The Commission treated the pipelines' intracorporate transfer of its own production as if it had been bought from another entity and determined its "cost" to the pipeline applying the same area or national rates the Commission applied to independently produced gas. The Commission determined the pipelines' sales price to its
533 customers on a cost-of-service basis.[1] ⊥

[1] Basically, cost-of-service pricing adds the costs required to operate and maintain the pipeline to the cost of both the gas purchased from independent producers and the gas produced by the pipeline itself, then calculates and includes an additional amount to allow reasonable return on the pipeline's investment. The Commission initially had determined the cost of pipeline production on a cost-of-service basis, but began applying area rates to pipeline production in 1969. However, it continued to price pipeline production from

The fuel shortages of the 1970s revealed two flaws in the regulation of gas production. The first appeared when the area and national rates established by the Commission for gas sold on the interstate market fell markedly below the price available for gas sold on the intrastate market, which was not regulated by the Commission. The price disparity between the two markets skewed the distribution of gas and resulted in shortages of gas available for interstate sale. *See Air Products & Chemicals, Inc. v. FERC*, 650 F.2d 687, 705 (5th Cir. 1981). The second became apparent when the area and national rates established by the Commission did not provide a sufficient incentive to encourage exploration for new sources of gas. *See Pennzoil Co. v. FERC*, 645 F.2d 360, 367 n.13 (5th Cir. 1981). These two problems resulted in enactment of the NGPA. While the NGPA did not disturb the Commission's jurisdiction over the prices a pipeline could charge its customers, it did take away from the Commission the right to fix most prices paid for the production of natural gas.

In the NGPA, Congress defined several categories of natural gas and set maximum lawful prices for the "first sale" in each. The pipelines claim that because Congress intended for the NGPA to apply to both pipeline and independent production, the Commission's order defining "first sale" conflicts with the NGPA.

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leases acquired prior to 1969 on a cost-of-service basis. *See Chicago v. FPC*, 458 F.2d 731 (D.C.Cir.1971), *cert. denied*, 405 U.S. 1074, 92 S.Ct. 1495, 31 L.Ed.2d 808 (1972). The Commission subsequently provided that pipeline production on old leases from wells begun after January 1, 1973, would receive nationwide rates. *See Shell Oil Co. v. FPC*, 520 F.2d 1061 (5th Cir.), *cert. denied*, 426 U.S. 941, 96 S.Ct. 2661, 49 L.Ed.2d 394 (1976). These exceptions to the application of area or national rates represent historical practices the effect of which is continually diminished as early wells cease producing gas. They do not affect our decision.

II.

The NGPA generally defines "first sale" as "any sale of any volume of natural gas," to a specified purchaser. 15 U.S.C. § 3301(21)(A). However, this general definition is subject to a qualified exception which is crucial to the issue presented here. The subsection following the general definition provides that "first sale" shall *not* include "the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof." 15 U.S.C. § 3301(21)(B).

In Order No. 58, the Commission assumed that the sale referred to by section 3301(21)(B) was a transfer by the pipeline to its customers. The Commission found that such a transfer was not a "first sale" unless the gas transferred was exclusively attributable to the pipeline's own production. Thus, it provided that if a pipeline commingled gas produced by it with gas produced by other entities, the pipeline was not entitled to NGPA prices for the gas it produced.

Because sales by pipelines are normally comprised of commingled gas, the Commission acknowledged that its regulation denied NGPA prices to virtually all pipeline produced gas and that FERC would retain jurisdiction under the NGA to set the price of such gas. The Commission justified its regulation because it intruded the least into state regulation and because it was less difficult to administer.

Under the NGA, regulation of retail sales by interstate pipelines, intrastate pipelines and local distribution companies had been committed to the states. The Commission

found that applying NGPA prices to such sales, particularly those by intrastate pipelines and local distribution companies, would supplant an area of regulation traditionally controlled by the states. The Commission also found that applying NGPA prices to pipeline customer sales of natural gas would disrupt the method it had traditionally used to factor transportation and other costs into the price charged for natural gas. Although treating the transfer from the production to the transportation ⊥ division of the pipeline as a first sale would have eliminated the problems noted by the Commission, the Commission declined to do so because it had not previously treated an intracorporate transfer as a sale.[2] 534

III.

We have previously recognized that "an agency's interpretation of its own statute is generally given deference . . . ." *Columbia Gas Development Corp. v. FERC*, 651 F.2d 1146, 1155 (5th Cir. 1981). We have also recognized that a greater degree of deference results from such factors as (i) a long standing interpretation which has not been disturbed by congressional action, *see International Brotherhood of Teamsters v. Daniel*, 439 U.S. 551, 566 n.20, 99 S.Ct. 790, 800, 58 L.Ed.2d 808 (1979); *Sanchez v. Schweiker*, 656 F.2d 966, 970 (5th Cir. 1981) (per curiam), (ii) the fact that "the interpretation concerns matters within the agency's expertise," *Adkins v. Hampton*,

[2] In Order No. 98, the Commission, acting under the NGA authority it had recognized in Order No. 58, established prices for interstate pipeline sales which come from mixed volumes of pipeline and independent producer gas. The Commission allowed pipelines whose production had previously been priced according to area or national rates to sell gas at NGPA prices. It refused, however, to extend NGPA prices to pipelines whose production had been priced on a cost-of-service basis.

586 F.2d 1070, 1073 (5th Cir. 1978); *accord Office of Consumers' Council v. FERC*, 655 F.2d 1132, 1141 (D.C. Cir.1980), and (iii) the fact that a contemporaneous interpretation of the statute suggests that the agency personnel interpreting the act had a hand in its development. *See Ford Motor Credit Co. v. Milhollin*, 444 U.S. 555, 100 S.Ct. 790, 797, 63 L.Ed.2d 22 (1980); *Phillips Petroleum Co. v. Wisconsin*, 347 US. 672, 689, 74 S.Ct. 794, 803, 98 L.Ed. 1035 (Douglas, J. dissenting). While the presence of these factors argues for greater deference, their absence suggests that a court need not accord as much deference as it otherwise would and indeed may rely on its own expertise in construing the intent of Congress. *See Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 42 n.27, 97 S.Ct. 926, 949, 51 L.Ed.2d 124 (1977); *Louisiana Chemical Association v. Bingham*, 657 F.2d 777, 779 (5th Cir. 1981).

In *Batterton v. Francis*, 432 U.S. 416, 425, 97 S.Ct. 2399, 2405, 53 L.Ed.2d 448 (1977), the Supreme Court recognized that when Congress "expressly delegated to [an agency] the power to prescribe standards" the resulting regulations should not be set aside by a court "simply because it would have interpreted the statute in a different manner." The Court distinguished legislative regulations, which are issued "pursuant to statutory authority and . . . implement the statute, as, for example, the proxy rules issued by the Securities and Exchange Commission," from merely interpretative regulations. *Id.* at 426 n.9, 97 S.Ct. at 2405 n.9. With respect to interpretative regulations, the Court noted that a lesser degree of deference is due, and stated "[v]arying degrees of deference are accorded to administrative interpretations, based on such factors as the timing and consistency of the agency's position and the nature of its expertise." *Id.*

Applying these factors to the present case, we find that the Commission's definition of "first sale" in Order No. 58 has not yet received the sanction which comes from long years of application by the agency and tacit congressional acceptance.[3] Moreover, this definition does not concern an area particularly within the agency's expertise. The Commission concedes that the concept of "first sale" is new to energy regulation, having been initially introduced by President Carter in a message to Congress. Defining this term does not bring into play the experience which the agency has gained in administering the NGA nor does this definition draw on the agency's expertise in dealing with the technical problems associated with energy regulation. The one factor which augments the deference due the Commission is its contemporaneous interpretation of the statute. The Commission ⊥ did have first-hand knowledge of the 535
problems leading to the passage of the NGPA. Yet, the weight of this factor is diminished since the Commission has admitted that it had no input into the development of the term "first sale." In sum, these factors fall far short of demanding a deference to the Commission's interpretation of the statute which could challenge the clear meaning of a statute as revealed by its language, purpose and history. *International Brotherhood of Teamsters v. Daniel*, 439 U.S. at 566 n.20, 99 S.Ct. at 800; *see Mohasco Corp. v. Silver*, 447 U.S. 807, 100 S.Ct. 2486, 2496, 65 L.Ed.2d 532 (1980); *Louisiana Chemical Association v. Bingham*, 657 F.2d 777, 779 (5th Cir. 1981).

IV.

"The starting point in every case involving the construction of a statute is the language itself." *International*

[3] 15 U.S.C. § 3411(b) authorizes the Commission "to define, by rule, accounting, technical, and trade terms used in this chapter."

Brotherhood of Teamsters v. Daniel, 439 U.S. at 558, 99 S.Ct. at 795. Sections 3311-3319 of the NGPA set a price for the "first sale" of natural gas in defined categories. Section 3301(21)(B) provides: (i) the sale of gas by a pipeline is not a "first sale," (ii) unless the sale was attributable to the pipeline's own production.

The first part of section 3301(21)(B) has a clear purpose. If its denial of "first sale" status to pipeline sales had not been included in the NGPA, pipelines which bought gas produced by independent producers and then resold it would have been involved in two "first sales," once as purchaser from the independent producer and then as seller to its customer. The restriction operates to eliminate this possibility by denying "first sale" status to the downstream sale.

The Commission's interpretation of section 3301(21)(B) would effectively read the second part of this subsection out of the NGPA. By over-stressing the first provision that sales by a pipeline are not first sales, the Commission would render the unless clause of subsection (B) a nullity. *See Ideal Mutual Insurance Co. v. C.D.I. Construction, Inc.*, 640 F.2d 654, 658 n.7 (5th Cir. 1981).

This second part of subsection (B) has a purpose equally as clear as the first. As we show below, NGPA contemplates that the pipeline is both a buyer and seller as to its own production. Blotting out the unless clause would mean the sale it makes of natural gas to itself in an intracorporate transfer would be excluded from NGPA in the same way the sale to its downstream customer is excluded. If this construction is placed on the Act, all natural gas produced by a pipeline would be denied "first sale" status under NGPA. Nothing in the language used here or elsewhere in the NGPA suggests any intent to deny NGPA pricing to

natural gas just because it is produced by a pipeline. To the contrary, the unless clause of subsection (B) can only have meaning if it is interpreted as granting "first sale" status to gas which is attributable to pipeline production. The pipeline's later sale of this gas to its customer would, of course, still be excluded from "first sale" treatment by the first part of the subsection.

The Commission claims that its interpretation of first sale is consistent with both the purposes of the statute and the legislative history. We disagree. Two of the overriding purposes of the NGPA were to eliminate the dual interstate and intrastate market for natural gas and to provide higher prices to encourage production. *See* H.R. Doc. No. 95-128, 95th Cong., 1st Sess. 5 (1977). Neither of these purposes is served by creating a distinction between pipeline and independent producers.

In achieving the goal of increasing natural gas production, pipeline producers deserve the price encouragement of NGPA no less than other producers. The Commission contends that it has encouraged increased production by extending NGPA prices to some pipeline producers in Order No. 98. This argument is sophistic. The Commission's duty is to administer the law Congress passed in light of the purposes for which it was passed. It is not an agency's prerogative to alter a statutory scheme even if its alteration is as good or better than the congressional one. The fact that ⊥ the agency gives back all or part of what it takes 536
from the law's grant in no way justifies departure from the congressional purpose in the first instance.

With respect to the goal of eliminating a dual market structure, the Commission's order would exclude virtually all interstate pipeline, intrastate pipeline and local distribution company production from the NGPA's uniform prices.

While the Commission would retain control of interstate pipeline production under the NGA, the effect of its order would be to leave intact state regulation of intrastate pipeline and local distribution company production. The intrastate market for such production would thus be perpetuated. This would leave a substantial vestige of the dual market structure Congress sought to eliminate.

The legislative history of section 3301(21) does not illuminate this issue. Congress did not explain its definition of first sale either in the committee reports that accompanied the various drafts of the NGPA or in the discussions that occurred in each house.

The Commission would support its interpretation by noting that the term "first sale" is used in a subchapter titled Wellhead Pricing and that first sales are referred to as "wellhead" or "field" sales in the legislative history. The Commission reasons that because a sale by a pipeline to its customer cannot be a wellhead sale, Congress must have intended to deny pipeline production first sale status. The Commission's Order No. 58 is inconsistent with this reasoning because it recognizes that non-wellhead sales may be first sales. Order No. 58 would allow as a first sale a downline sale to a pipeline customer if the sale was exclusively attributable to pipeline production despite the fact that such a sale is no more a wellhead sale than is any other pipeline customer sale.

More importantly, the legislative history noted by the Commission conflicts with a premise which underlies Order No. 58. The Commission asserts that a problem is created by extending first sale status to pipeline production. The problem it perceives derives principally from its assumption that the first sale by the pipeline producer must be the sale to a customer downline. The legislative history equat-

ing a first sale with a wellhead or field sale suggests, however, that Congress intended the sale by the producer of the gas to be the first sale. In the context of pipeline production, this would mean that the intracorporate transfer from the production division of the pipeline to the transportation division of the pipeline would constitute the first sale. If the Commission had equated this intracorporate transfer with the acquisition of pipeline gas from an independent producer the "problems" it perceived and sought to solve in Order No. 58 would not have arisen.

Other provisions in the statute and such relevant legislative history as does exist persuade us that Congress both intended to accord pipeline production first sale status and contemplated that the intracorporate transfer would be treated as a first sale. Subchapter II of the NGPA provides for incremental pricing by the pipelines. Congress directed that pipelines pass through to certain industrial users the higher first sale acquisition costs paid by the pipelines for natural gas under NGPA. In defining first sale acquisition costs, Congress stated that the cost would be the price paid in any first sale. *See* 15 U.S.C. § 3343(b)(1)(A). Additionally, Congress provided that for "any natural gas produced by any interstate pipeline or any affiliate of such pipeline, the first sale acquisition cost of such gas shall be determined in accordance with rules prescribed by the Commission." 15 U.S.C. § 3343(b)(2). By referring to the "first sale acquisition cost of *such* gas," in terms of "any gas produced by any interstate pipeline," Congress must have contemplated that any gas produced by a pipeline would be subject to a first sale. Moreover, the fact that Congress provided that the "first sale acquisition cost" of pipeline produced gas would, like the first sale price paid to independent producers, be passed along to the pipeline's ultimate customers suggests that both prices were to be

537 treated in a similar manner. Congress contemplated that the first sale acquisition cost for both pipeline and independent production would be treated as the cost of the gas to the pipeline in determining, under the cost-of-service method, the price charged by the pipeline. The first sale thus appears to refer to the intracorporate transfer.

The Commission contends that if Congress had intended pipeline production to be subject to first sales, it would not have treated pipeline production separately from other production for which there is a "price paid." This distinction, however, merely reflects Congress' awareness that technically an intracorporate transfer involves no price paid. It would appear that Congress intended for the Commission to apply NGPA prices as the "cost" of this gas to the pipeline, just as the Commission had applied area and national rates under the NGA to determine the "cost" to the pipeline of pipeline produced gas.

Support for the proposition that the intracorporate transfer constitutes a first sale is contained in the conference committee report. In discussing the Commission's power to define terms in the NGPA, the Committee stated:

> the Commission may define terms such as "transfer for value" used in the definition of first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition.

H.R.Rep. No. 95-1752, 95th Cong., 2d Sess. 116, *reprinted in* [1978] U.S.Code Cong. & Ad.News 8800, 9033. The Commission contends that this statement only suggests that the Commission may issue regulations defining an intracorporate transaction as a first sale, not that it is required to do so. We reach a different conclusion. This comment assumes that intracorporate transactions will fall

within the first sale definition. The decision which Congress committed to the Commission's judgment was whether regulations were necessary to govern those transactions. The fact that the Commission was permitted to regulate intracorporate transactions under the first sale definition does not imply that Congress did not intend in the first instance for them to be treated as first sales.

Treating this transfer as a first sale would obviate the difficulties which prompted the Commission to promulgate Order No. 58. The Commission had been concerned that normally only a portion of a sale by a pipeline to its customers downline would be attributable to the pipeline's own production. Because only a portion of the sale, rather than the sale itself, would be attributable, the Commission reasoned that a sale downline could not be a first sale under the terms of the NGPA unless it were comprised exclusively of pipeline produced gas. However, treating the intracorporate transfer as a first sale would mean that that sale would be wholly attributable to the pipeline's production.

The Commission was also concerned that applying NGPA prices to sales to customers downline would supplant the state's traditional jurisdiction over retail sales by interstate pipelines, intrastate pipelines and local distribution companies. However, if the NGPA prices attached to the intracorporate transfer by the producer then the state's jurisdiction over retail sales would remain intact. The only change would be that the cost of the gas to the pipeline or distribution company would be the NGPA price. Jurisdiction to set the final retail charge would remain with the state. Although the retail price would reflect the NGPA cost of gas, that change is consistent with Congress' desire to establish a uniform price for producers of both intrastate and interstate gas.

Finally, the Commission was concerned that applying NGPA prices to the sale downline would disturb its traditional method of establishing the cost of gas sold by the pipeline. The Commission feared that the new downline sale price would be limited to the maximum NGPA price rather than reflecting its traditional costs-plus-a-reasonable-return methodology. This would create difficulty in factoring in the costs of operating and maintaining the pipeline. However, if the NGPA prices were applied to the intracorporate transfer, then the Commission's practice would
538 not be disturbed. ⊥ Treating the intracorporate transfer as a first sale would establish the "cost" of the pipeline's own production to the pipeline at NGPA prices, just as the cost of independently produced gas to the pipeline is calculated. This cost could then be factored in as a component of the pipeline's costs, precisely as the Commission has done under the cost-of-service method. This is in fact what the Commission proposed to do in Order No. 98 and what it had previously done when it applied area and national rates to both independent and pipeline production.

FERC, however, refused to treat this intracorporate transfer as a first sale because it maintained that no sale took place. FERC also noted that because no contracts govern the intracorporate transfer, certain administrative problems would result. Although the legislative history convinces us that Congress intended the intracorporate transfer to be treated as a first sale, we respect the Commission's determination that administration would be difficult. We note, however, that in Order No. 98 the Commission would apply NGPA prices to this same intracorporate transfer. This assures us that the Commission's authority to issue regulations to govern this area will enable it to overcome these difficulties.

V.

Relying on the language, purposes and history of the NGPA, we hold that Congress clearly intended for any production attributable to an "interstate pipeline, intrastate pipeline or local distribution company, or any affiliate thereof" to be accorded first sale status under the NGPA and that Congress contemplated that the intracorporate transfer of pipeline production to the pipeline would be treated as the first sale. We therefore vacate Order No. 58. Because we hold that the Commission lacked authority to set prices for interstate pipeline production under the NGA, we also vacate Order No. 98 without reaching the issues of arbitrary pricing raised here.[4]

Orders Nos. 58 and 98 are

VACATED.

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[4] Northwest Pipeline Corporation petitioned for review of the Commission's decision in Order No. 98 to terminate its "special circumstances exception," which would have allowed a pipeline producer to seek a higher price than the nationwide rate set by the Commission under the NGA. The effect of our holding with respect to Order No. 58 is that the price for pipeline production will now be set under the NGPA. The parties have noted in their briefs that there is an ongoing rulemaking on the subject of such special relief under the NGPA. The issue raised by Northwest is therefore not yet ripe for review.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Charles B. Curtis, *Chairman;* Georgiana Sheldon, Matthew Holden, Jr., and George R. Hall.

Final Rule Governing the Maximum Lawful Price for Pipeline, Distributor or Affiliate Production) Docket No. RM80-7

ORDER NO. 58

FINAL REGULATIONS
(Issued November 14, 1979)

I. Background

On December 1, 1978, the Federal Energy Regulatory Commission (Commission) issued interim regulations (43 F.R. 56448, December 1, 1978) implementing the Natural Gas Policy Act of 1978 (NGPA). Section 270.203(a) of the interim regulations implements section 2(21)(B) of the NGPA and prescribes which sales of natural gas will be considered to be first sales for NGPA purposes because the gas is attributable to production by interstate pipelines, intrastate pipelines, local distribution companies and affiliates thereof. Section 270.203(b) of the interim regulations defines what other sales by these entities will be considered to be first sales in order to prevent circumvention of the maximum lawful prices established under the NGPA. Section 270.203(c) of the interim regulations defines certain terms used in §270.203.

The Commission has received numerous comments concerning §270.203 and is amending that section based on an analysis of these comments. Section 270.203 as amended delineates the circumstances under which a sale of

production of an interstate or intrastate pipeline, local distribution company (or affiliate of any of these entities) will be regulated as a first sale under the NGPA. Production of interstate pipelines and their affiliates which is not regulated as a first sale under the NGPA is subject to continuing regulation under the Natural Gas Act (NGA). In response to comments received on §270.203 and in conjunction with the amendments issued in this order, the Commission is proposing by separate order to add a new §2.66a to its regulations under the NGA which, in general, will permit interstate pipelines to determine the cost component associated with their own production by reference to NGPA maximum lawful prices, for NGA ratemaking purposes, in those instances where the pipeline would have been allowed the area or national rates under the NGA.

II. Summary of Comments and Revisions to §270.203

A. Attribution Rule for Pipelines and Distributors

Section 2(21)(B) of the NGPA provides that a sale of natural gas by a pipeline, distributor or affiliate thereof is not a first sale unless the sale is "attributable" to volumes of natural gas produced by such pipeline, distributor or affiliate thereof. Section 270.203(a), as amended, describes the circumstances under which a sale of natural gas will be considered to be a "first sale" of natural gas "attributable" to volumes produced by a pipeline or distributor. Under the amended rule sales by affiliates of pipelines and distributors are now treated separately in §270.203(c). Section 207.203(a) has been clarified to indicate that, to the extent a sale is comprised *exclusively* of production volumes from identifiable wells, properties, or reservoirs which are owned by the pipeline or distributor making the sale, such sale is attributable to volumes of natural gas produced by that pipeline or distributor. For example, if a pipeline were to sell its production at the wellhead, in an offsystem sale, such a sale would generally qualify under §270.203(a) as a first sale.

As the comments point out, however, sales by pipelines usually do not occur at the wellhead. Pipeline sales generally occur at the point the natural gas is withdrawn from the pipeline's general system supply. Furthermore, pipelines usually commingle the gas they produce with gas purchased from other sources and sell such mixed volumes without regard to the source of the particular volumes of natural gas involved. The Commission is aware that, as a result, most sales by interstate pipelines will not qualify as first sales under §270.203(a) because the volumes sold are not produced exclusively by and identifiable to the pipeline's own production.

It should be noted, however, that were a pipeline to dedicate natural gas which it produced from an identifiable source to a particular purchaser by contract, commingle the gas with general system supply gas and withdraw equivalent volumes for delivery to that purchaser the sale would generally qualify as a first sale. The sale would qualify because the source of the gas involved is identified and the Commission could be assured that the gas is "attributable" to the pipeline's own production. In addition, the Commission would be able to evaluate requests for allowances for transportation and storage expenses incurred between the wellhead and the point of delivery to the purchaser.

Although many comments have recommended otherwise, the Commission will not interpret the term "attributable" so as to confer first sale treatment on pipeline sales if only a portion of the gas involved was produced by the pipeline. The language of section 2(21)(B) requires that a sale be "attributable" to the pipeline's *own* production. We believe that Congress did not intend for pipeline or distributor sales from general system supply to qualify as "first sales" merely because some portion of that supply, no matter how small, consists of its own production. Rather, we believe that these sales were precisely the type of sales

which were intended to qualify for the general exclusion from first sale regulation for pipeline or distributor sales in section 2(21)(B) of the NGPA. The attribution rule accomplishes that result.

Assuming we were to interpret section (2)(21)(B) to treat such mixed volume sales by pipelines or distributors as first sales, the Commission would not adopt such a course because it would result in a wholly inappropriate and unworkable dividing line between "first sales" and other sales, and would override the existing division between Federal and State authority relating to gas sales by pipelines and distributors. The Commission believes that Congress intended that section 2(21) of the NGPA disturb resale rate regulation under the NGA as little as possible. Under the NGA the Commission only has authority to regulate the wholesale rates of interstate pipelines. Retail sales by interstate pipelines, intrastate pipelines and local distribution companies have traditionally been regulated by the States. If the Commission were to treat all pipeline or distributor sales as first sales where any portion of the volume sold is produced by the pipeline or distributor, Commission regulation would extend to retail sales by interstate pipelines to their direct sale industrial customers. The Commission would also be exercising "first sale" jurisdiction over sales by intrastate pipelines and local distributors of volumes produced by these companies. Yet, pipelines and distributors that did not produce any portion of the natural gas involved in their sales would continue to be exempt from first sale regulation under the exclusion in section 2(21)(B) of the NGPA. Moreover, a pipeline or distributor would be able to incur or avoid first sale regulation by entering into production activities or abandoning production activities as it saw fit. The Commission declines to effect such results absent a clearer showing of a need to do so.

Furthermore if the Commission were to treat all sales as first sales where any portion of the volumes sold is produced by a pipeline or distributor, additional problems would be created in regard to mixed volume sales by pipelines. Where a pipeline makes a sale from general system supply rather than at the wellhead, the source of the particular volumes of gas sold generally cannot be determined. Although comments by pipelines request first sale treatment for such sales they also request allowances for non-production related costs such as transportation and storage which are incurred between the wellhead and the point at which the volumes are delivered to the purchaser and the sale occurs. However, if mixed volume sales by pipelines and distributors were considered to be first sales, the Commission would be unable to reasonably act on such requests for allowances since the source of the particular volumes of gas involved in any given sale could not be determined.

For the reasons stated above, the Commission has decided to limit first sale treatment for pipelines and distributors under the attribution rule to those sales which are statutorily designated as first sales because the volumes sold are exclusively attributable to the pipeline or distributor's production.

Many comments recognize the problems inherent in according first sale treatment to mixed volume sales by pipelines. As an alternative, these comments suggest that the Commission accord first sale treatment to the pipeline's production by imputing a sale at the point where the pipeline takes its gas into its transmission system. However, imputing a sale at the wellhead would extend the first sale concept to intracorporate transactions. As a result, Title I prices would be applied to bookkeeping and accounting entries of a corporation rather than to actual sales. In addition, such a rule would extend NGPA first sale jurisdiction to all corporations which produce their own natural gas. Comments filed by industrial corporations

which consume their own natural gas production indicate that this would produce undesirable results and that no valid regulatory purpose would be served by extending the Commission's jurisdiction to cover such production. These comments suggest that such an extension could discourage industrial self-help measures and would contravene the policy expressed in section 608 of PURPA. The Commission agrees that no valid reason presently exists to define intracorporate transfers of gas at the wellhead by intrastate pipelines and distributors as sales. Indeed, to do so would displace existing State regulation of these companies and their production. The Commission declines to effect such results.

B. **Circumvention Rule for Pipelines and Distributors.**

Pursuant to its authority under section 2(21)(A)(v) of the NGPA the Commission has defined certain sales by pipelines and distributors, in §270.203(b), as first sales in order to prevent circumvention of the NGPA maximum lawful prices. Section 207.203(b), as amended, provides that any sale by a pipeline or distributor which is comprised of production volumes from properties owned by the pipeline or distributor and production volumes from other sources will be considered to be a first sale unless one of two exclusions under the rule applies. The first exclusion provides that if the rate at which such natural gas is sold by the pipeline or distributor is regulated under the NGA or is regulated or subject to regulation by a State agency empowered by State statute to establish, modify or set aside the rate for the sale, then the sale will not be considered to be a first sale under the circumvention rule. The second exclusion provides that a sale by a pipeline or distributor will not be considered to be a first sale under the circumvention rule if the Commission, upon application, has determined not to treat the sale as a first sale. The Commission intends to waive first sale treatment under the circumvention rule, pursuant to the second exclusion, only

where the applicant has presented sufficient facts to establish that first sale treatment is not needed to prevent circumvention of the NGPA maximum lawful prices. Any application received pursuant to §270.203(b)(2) will be noticed in the *Federal Register*, and interested parties will be given an opportunity to comment on the merits of the application.

The circumvention rule for pipelines and distributors is a necessary corollary to the attribution rule. Under the attribution rule, sales by pipelines or distributors are considered to be "attributable" to production by the pipeline or distributor, and thus to be first sales, only where the sale is comprised exclusively of the pipeline or distributor's own production. Mixed volume sales by a pipeline or distributor are not considered to be first sales under the attribution rule. Accordingly, a pipeline or distributor could avoid first sale treatment and circumvent the maximum lawful prices established by the NGPA merely by making mixed volume sales. Section 270.203(b) prevents such circumvention of NGPA prices by regulating mixed volume sales as first sales unless they are subject to other safeguards; *e.g.*, regulation under the NGA, regulation by a State agency, or review by the Commission, on application, in order to determine whether a sale should be treated as a first sale.

Section 270.203(b) avoids the potential for recreating a dual market such as existed under the NGA. By prescribing maximum lawful prices for natural gas without regard to the situs of the sale, Congress sought to eliminate advantages enjoyed by the intrastate market. However, because a sale of mixed volumes would not be "attributable" to a pipeline's own production within the meaning of §270.203(a), such a sale would not be regulated as a first sale under the NGPA. In those instances where the sale would not be regulated under the NGA or by any particular State, the sale price would not be regulated at all.

By continuing to commingle its production with gas purchased from others, the pipeline or distributor could charge prices in excess of those charged by other sellers and could use the increased revenues to pay higher royalties in order to secure additional leases. The pipeline or distributor would have an incentive to make mixed volume sales in a State which did not regulate the price for such sales so that it could secure such an advantage over other producers in securing leases. In order to avoid such a result, §270.203(b) makes such sales of otherwise unregulated gas first sales unless the Commission, on application, decides that first sale treatment is not necessary in order to prevent circumvention of the NGPA maximum lawful prices.

Some of the comments received by the Commission assert that, while the individual States are given the power in section 602 of the NGPA to set ceiling prices below the NGPA price ceilings, the Commission was only given the authority to create higher ceiling prices and has unlawfully attempted in §270.203 to establish lower ceiling prices indirectly by precluding application of NGPA maximum lawful prices. These comments have misconstrued the effect of §270.203. In §270.203(a) the Commission has interpreted the term "attributable" as that term is used in section 2(21)(B) of the NGPA and has described which sales by pipelines and distributors are attributable to their own production and are, thus, first sales. The Commission believes that its definition of the term "attributable" is the most reasonable and advisable one based on the policies articulated above. The fact that the Commission did not exercise its authority under section 2(21)(A)(v) of the NGPA to subject all pipeline or distributor sales to first sale treatment does not mean that the Commission has set ceiling prices below the NGPA ceiling prices in contravention of section 602 of the NGPA. In fact, in §207.203 the Commission has exercised its authority under section 2(21)(A)(v) of the NGPA to increase the number of sales which will be governed by the NGPA maximum lawful prices.

C. Sales by Certain Affiliates of Pipelines or Distributors

Pursuant to our interpretation of the term "attributable" as it is used in section 2(21)(B) of the NGPA and our authority under section 2(21)(A)(v) of the NGPA, the Commission in §270.203(c), has provided that any sale by an affiliate of a pipeline or distributor is a first sale if such affiliate is not itself a pipeline or distributor unless the Commission, upon application, has decided not to treat such sale as a first sale. The Commission has also made clear that the term "sale" as it is used in §270.203(c) does not include any transaction between an interstate pipeline and an affiliate thereof if such transaction would not have been treated as a sale for purposes of the NGA.

The Commission has exercised its authority under section 2(21)(A)(v) of NGPA, in §270.203(c), to define all such affiliate sales as first sales in order to prevent circumvention of the NGPA maximum lawful prices. The Commission has adopted this approach for the following reason. Sales by affiliates of pipelines and distributors are excluded from first sale treatment by section 2(21)(B) of the NGPA unless such sales are "attributable" to the affiliate's own production. As a result, sales by gatherers who are affiliated with a pipeline or distributor would be excluded from first sale treatment where the gatherer did not produce all of the gas sold, irrespective of whether the gatherer was or was not selling the gas to the affiliated pipeline or distributor. However, sales by gatherers that are *not* affiliated with a pipeline or distributor would not be excluded from first sale treatment. Moreover, an entity selling natural gas could avoid first sale treatment and circumvent the maximum lawful prices established by the NGPA merely by being an affiliate of a pipeline or distributor and conducting transactions which would not otherwise qualify as first sales under §270.203(a). Accordingly, the Commission has found it necessary to define all sales by affiliates of a pipeline or distributor as

first sales if the affiliate is not itself a pipeline or distributor.[1] However, under §270.203(c) the Commission will entertain applications in individual instances to allow an applicant to present sufficient facts to establish that such first sale treatment is not necessary to prevent circumvention of the NGPA prices.

Treating all affiliate sales as first sales if the affiliate is not itself a pipeline or distributor does no more than recognize what section 2(21) and the other provisions of the NGPA appear to provide for: first sale treatment for all sales which precede sales by pipeline or distributors, where the seller is not a pipeline or distributor. Furthermore, the rule in §270.203(c) is supported by the desirability of extending Title I maximum lawful prices and related provisions of our regulations concerning resales (§270.202) and sales of natural gas subject to differing maximum lawful prices (§270.201), and by the need to avoid the anomalous results which would follow from failing to define these sales as first sales.

D. **Reports**

Section §270.203(d), as amended, requires a pipeline or distributor to file a report with this Commission every six months showing the price charged in sales which have been excluded from first sale treatment under §270.203(b)(2) and (c). These reports will allow the Commission to re-evaluate those sales in order to determine whether they should be treated as first sales in order to prevent circumvention of the maximum lawful prices established by the NGPA.

E. **Definitions**

Section 270.203(e) defines certain terms as they are used in §270.203. "Pipeline or distributor" is defined as an interstate pipeline, an intrastate pipeline or a local

[1]See Notice of Proposed Rulemaking issued with this order discussing requirement that an interstate pipeline secure abandonment authorization prior to spinning off production properties to an affiliate.

distribution company. "State Agency" is defined as a State, a political subdivision of a State, or an agency or instrumentality of either.

III. PUBLIC PROCEDURES AND EFFECTIVE DATE

The regulations in Part 270 were originally proposed for comment in November of 1978 and issued as interim regulations on December 1, 1978 (43 F.R. 56448, December 1, 1978). For 60 days thereafter comments were received and during that period public hearings were held on these regulations. By this process the Commission complied with the provisions of section 502(b) of the NGPA, which requires that "[t]o the maximum extent practicable," an opportunity for the oral presentation of the data, views, and arguments be afforded for certain regulations under the NGPA. The amendments to §270.203 contained in this order rest upon consideration given to the information received during the above-described notice, comment, and hearing process, as well as upon comments received via the FERC "Hot Line." The Commission finds that further notice and public procedure with respect to these rules is unnecessary. The Commission also finds that good cause exists to make these regulations effective immediately. Delay in the effective date of these regulations, even for a short period of time, may cause pipelines, distributors or their affiliates to postpone, or forego altogether, drilling decisions which would increase the nationwide availability of natural gas. Thus, the Commission is dispensing with the publication requirements of 5 U.S.C. §553(d)(1).

(Natural Gas Policy Act of 1978, 15 U.S.C. 3301 *et seq.*; Natural Gas Act, as amended, 15 U.S.C. 717 *et seq.*; Department of Energy Organization Act, 42 U.S.C. 7107 *et seq.*; E.O. 12009, 42 F.R. 46267).

In consideration of the foregoing §270.203 of Part 270, Subchapter H, Chapter I, Title 18, Code of Federal

Regulations is issued as a final regulation as set forth below, effective immediately.

By the Commission.

(SEAL)

Kenneth F. Plumb,
Secretary

1. Part 270 is amended in the table of contents and in the text of the regulation by deleting §270.203 and substituting the following in lieu thereof:

§270.203 **Pipeline, distributor and affiliate production.**

(a) **Attribution rule for pipelines and distributors.** For purposes of applying section 2(21)(B) of the NGPA, a sale by a pipeline or distributor is a sale of natural gas attributable to volumes of natural gas produced by such pipeline or distributor to the extent that such sale is comprised exclusively of production volumes of natural gas from identifiable wells, properties, or reservoirs which are owned by such pipeline or distributor.

(b) **Circumvention rule for pipelines and distributors.** In order to prevent circumvention of the maximum lawful prices established under Title I of the NGPA, the term, "first sale" includes any sale by a pipeline or distributor which is comprised of production volumes from identifiable wells, properties, or reservoirs if a portion of those volumes is produced from wells, properties, or reservoirs owned by such pipeline or distributor unless:

(1) the price at which such natural gas is sold is regulated pursuant to the Natural Gas Act or is regulated by a State agency empowered by State statute to establish, modify or set aside the rate for such sale; or

(2) the Commission, on application, has determined not to treat such sale as a first sale.

(c) **Sales by certain affiliates.** Any sale by an affiliate of a pipeline or distributor is a first sale if such affiliate is not

itself a pipeline or distributor, unless the Commission, on application, has determined not to treat such sale as a first sale. For purposes of this paragraph, the term "sale" does not include any transaction between an interstate pipeline and an affiliate thereof if such transaction would not have been treated as a sale for purposes of the Natural Gas Act.

(d) **Reports.** A pipeline, distributor or affiliate thereof must file a report with this Commission every 6 months showing the price charged in a sale which was excluded from first sale treatment under paragraph (b)(2) or (c) of this section. Any determination under paragraph (b)(2) or (c) may be revoked by the Commission on the basis of information in such reports or on the basis of other information.

(e) **Definitions.** For the purposes of this section:

(1) "Pipeline or distributor" means an interstate pipeline, an intrastate pipeline, or a local distribution company.

(2) "State agency" means a State, a political subdivision of a State, of any agency or instrumentality of either.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Title 18 - Conservation of Power and Water Resources

Part 2 - General Policy and Interpretations

Part 154 - Rate Schedule and Tariffs

Part 270 - Rules Generally Applicable to Regulated Sales of Natural Gas

FINAL RULE GOVERNING PRICE OF PIPELINE PRODUCTION UNDER THE NATURAL GAS ACT

(Docket No. RM80-6)

ORDER NO. 98

(Issued August 4, 1980)

AGENCY: Federal Energy Regulatory Commission.

ACTION: Final Rule.

SUMMARY: Under section 2(21)(B) of the Natural Gas Policy Act of 1978 (NGPA) and §270.203 of the Commission's regulations, sales of natural gas by pipelines or distributors are not first sales, and thus not subject to NGPA prices, unless the gas is comprised exclusively of production volumes of natural gas from identifiable wells, properties or reservoirs that are owned by the pipeline or distributor. Therefore, sales of volumes of interstate pipeline production that are commingled with purchased gas prior to sale remain subject to the Commission's pricing authority under the Natural Gas Act (NGA).

The Commission is adopting regulations under the NGA governing the pricing of interstate pipeline production sold in mixed volume sales. These regulations continue the Commission's policy of parity of treatment by permitting pipeline production that is now priced by reference to the maximum lawful price that would have been applicable under Title I of the NGPA if the gas had been sold in a first

sale. Natural gas that is now priced on a cost-of-service basis will continue to be subject to the cost-of-service pricing treatment.

EFFECTIVE DATE: The final rule is effective [30 days after date of issuance.]

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UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Charles B. Curtis, *Chairman;* Georgiana Sheldon, and George R. Hall.

Final Rule Governing Pricing of Pipeline Production Under the Natural Gas Act	))))	Docket No. RM80-6

ORDER NO. 98

FINAL RULE

(Issued August 4, 1980)

I. Introduction.

A. Statutory Framework

Interstate pipelines in addition to transporting gas owned by others, acquire gas and sell it to their customers, either by purchasing it or by producing it themselves. Under the Natural Gas Policy Act of 1978 (NGPA), if gas is sold to an interstate pipeline in a first sale,[1] the producer (or other

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[1]First sale is defined in section 2(21) of the NGPA of the NGPA as follows:

(21) FIRST SALE—

(A) GENERAL RULE-The term "first sale" means any sale of any volume of natural gas—

(i) to any interstate pipeline or intrastate pipeline;

(ii) to any local distribution company;

(iii) to any person for use by such person;

(iv) which precedes any sale described in clauses (i), (ii), or (iii); and

(v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this Act.

(B) CERTAIN SALES NOT INCLUDED—Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

seller) may sell it to the pipeline at the NGPA ceiling price.[2] When the interstate pipeline sells gas acquired in a first sale, the NGPA's "guaranteed passthrough" provision precludes the Commission from denying passthrough of the acquisition cost of the gas (if below the applicable NGPA ceiling) unless the amount paid was excessive due to fraud, abuse of similar grounds.[3] On the other hand, if the pipeline does not acquire the gas in a first sale, neither the NGPA ceiling prices nor the "guaranteed passthrough" provision applies.

Section 2(21) of the NGPA and Order No. 58[4] define the circumstances under which a pipeline's acquisition of natural gas would be treated as a first sale. As a general matter, if the gas is acquired from another pipeline or from a distributor it is not a first sale.[5] If the gas is acquired from a person (other than a pipeline or distributor), whether affiliated or unaffiliated with the interstate pipeline, the gas is acquired in a first sale and both the NGPA ceiling prices

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[2]The NGPA ceiling prices are deemed just and reasonable for purposes of the NGA (Section 601(b) of the NGPA). However, a buyer may insist on his contractual rights to purchase at a lower price (Section 101(b)(9) of the NGPA), and contractual authorization may be required in the case of first sales that remain subject to the NGA. *See* Order No. 23 (Docket No. RM79-22, issued March 13, 1979), 44 Fed. Reg. 16895 (March 20, 1979); Order No. 23-A (issued June 12, 1979), 44 Fed. Reg. 34472 (June 15, 1979); Order No. 23-B (issued June 21, 1979), 44 Fed. Reg. 38834 (July 3, 1979).

[3]NGPA Section 601(c). In addition, the affiliated entities limitations may limit the extent of passthrough. *See* NGPA section 601(b)(1)(E).

[4]Order No. 58 (Docket No. RM80-7, issued November 14, 1979), 43 Fed. Reg. 66577 (Nov. 20, 1979). §270.203.

[5]NGPA Section 2(21)(B). Sales by pipelines or distributors of volumes comprised in whole or in part of their own production are first sales under certain circumstances. *See* §270.203(a) and (b); *see also, infra* note 7-9 and accompanying text.

and the "guaranteed passthrough" provision apply.[6] Thus, as more fully described below, if a pipeline's producing affiliate sells to the pipeline, that sale is a first sale; on the other hand, if gas acquired by a pipeline is produced from wells owned directly by the pipeline, there is neither a first sale to the pipeline under Order No. 58 nor a guaranteed passthrough. In the case of an interstate pipeline acquiring gas other than in a first sale, both the acquisition and sale are governed by the Natural Gas Act (NGA).

This rulemaking, commenced contemporaneously with the issuance of Order No. 58, addresses the Commission's policy under the NGA respecting gas acquired (other than in a first sale) by an interstate pipeline from its own production.

B. Pipeline and Affiliate Production

In addition to determining the circumstances under which a pipeline's acquisition of natural gas is a first sale, Section 2(21) of the NGPA also determines which sales by pipelines or distributors are first sales under the NGPA. Subparagraph (B) of Section 2(21) provides that first sales "shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or an affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or affiliate thereof." The Commission in Order No. 58 interpreted the word "attributable" to mean "comprised exclusively of production volumes of natural gas from identifiable wells, properties, or reservoirs which are owned by such pipeline or distributor."[7]

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[6]Sales by unaffiliated sellers (other than pipelines,distributors or their affiliates) are not barred from first sale treatment under section 2(21)(B). Sales by affiliates (other than pipelines or distributors) are first sales unless the Commission determines otherwise. *See* §270.203(c).

[7]See §270.203(a).

However, only a limited amount of pipeline or distributor owned production is committed from an identifiable source or is otherwise sold in a sale comprised exclusively of pipeline or distributor owned production. More typically, a pipeline will commingle its own production volumes with purchased gas and make mixed volume sales from its general system supply. Because such mixed volume sales generally would not be first sales,[8] they are not subject to the NGPA and Title I maximum lawful prices. Therefore, most sales of pipeline production remain subject to rate regulation under otherwise applicable Federal and state law: intrastate pipelines and local distribution companies are subject to existing state and local regulatory authority,[9] and interstate pipelines continue to be subject to price regulation under the NGA.

In conjunction with Order No. 58, the Commission issued a Notice of Proposed Rulemaking in exercise of its

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[8]A mixed volume sale by an intrastate pipeline that is not regulated by a state agency empowered by State statute to establish, modify or set aside the rate for such a sale is denominated by the Commission as a first sale, unless the Commission, on application, has determined not to treat such a sale as a first sale. §270.203(b). Such a sale is a first sale by exercise of the Commission's authority under section 2(21)(A)(v). *See infra* note 9 and accompanying text.

[9]Section 2(21)(A) of the NGPA, which expressly denominates certain sales as first sales, also empowers the Commission to extend the first sale definition to embrace any other sale in order to avoid circumvention of the NGPA maximum lawful prices. In Order No. 58, the Commission asserted this authority to include as first sales, sales by intrastate pipelines and local distributors that are not subject to state or NGA regulatory authority. *Mimeo* at 8-9; *see* §270.203(b). Also pursuant to section 2(21)(A)(v) the Commission will treat as first sales, sales by non-producing affiliates of pipelines or distributors, such as brokers or gatherers, which are not subject to Commission jurisdiction and are largely unregulated by the states. *Mimeo* at 12-13; §270.203(c). This limited exercise of the Commission's circumvention authority under Section 2(21)(A)(v) reflects our view that the NGPA pricing policies can be effectuated without disrupting any existing regulation of intrastate pipeline and distributor rates for mixed volume sales.

continuing authority under the NGA to establish rates for mixed volume sales of natural gas by interstate pipelines.[10] In order to achieve parity of pricing treatment among independent producers subject to Title I maximum prices and pipeline producers subject to NGA pricing authority, the proposed rule permitted a pipeline, in determining its NGA cost-of-service for mixed volume sales, to value its own production by reference to the Title I maximum lawful prices that would have been applicable to the gas had it been sold in a first sale. After review of public comments,[11] the Commission is adopting as final regulations the proposed amendments to the Commission's regulations under the NGA, to provide for parity of price treatment among independent and pipeline producers.[12]

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[10]Notice of Proposed Rulemaking (issued November 14, 1979); 44 Fed. Reg. 66612 (Nov. 20, 1979).

[11]Comments were timely filed by American Gas Association (AGA), Natural Gas Pipeline Company of America (Natural), Consolidated Gas Supply Corporation (Consolidated), Northwest Pipeline Corporation (Northwest), El Paso Natural Gas Company (El Paso), Northern Natural Gas Company (Northern), United Gas Pipe Line Company (United), Colorado Interstate Gas Company (CIG), Kentucky-West Virginia Gas Company (Kentucky-West Virginia), and the Kansas State Corporation Commission (Kansas). Comments were received after the close of the comment period from the Public Service Commission of the State of New York (New York), Southern Natural Gas Company (Southern), Sonat Exploration Company (Sonat) and Columbia Gas Transmission Company (Columbia). These comments are considered as if timely filed. However, we have not considered late comments received June 23, 1980, after the Commission meeting in which this final rule was considered, from Arizona Power Cooperative and the City of Wilcox, Arizona.

[12]The Commission is presently reviewing applications for rehearing of Order No. 58 and is further considering the policy underlying that Order. The issuance of this rule, which is predicated on the interpretation of section 2(21)(B) reflected in Order No. 58, does not dispose of those petitions for rehearing. Because the policies set out in both these dockets are firmly interlaced, we prefer to consider the legal and policy issues raised on rehearing of Order No. 58 in connection with consideration of any arguments raised in petitions for rehearing of these final regulations. *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968).

III. Background: Pricing Parity for Pipeline Producers Prior to the NGPA.

The pricing of pipeline production under th NGA is a question of policy that was originally addressed in the context of the Federal Power Commission's (FPC's) efforts to establish just and reasonable rates for producer sales of natural gas to the interstate market. Initially, the FPC determined producer rates by use of the cost-of-service methodology traditionally employed in determining rates for interstate pipelines. Subsequently, the FPC rejected that ratemaking method for sales by independent producers and off-system sales by pipeline producers and instead adopted a series of average cost-based rates which were applicable to such sales of gas produced in specified geographic areas. However, the area rates were not made applicable to pipeline production sold in mixed volume sales, so that the value of production transmitted from a pipeline's own producing operation continued to be included as a cost component in the pipeline's overall cost-of-service and was computed generally on the same test year basis as other elements of the cost-of-service. Test year projections were made for lease acquisition, exploration, development, and production.[13]

Subsequently, in Opinion No. 568,[14] the FPC rejected the cost-of-service ratemaking methodology for determining rates for pipeline production, finding that the economic and administrative considerations which had urged the abandonment of cost-of-service ratemaking for independent producers were equally as compelling in the

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[13] *City of Chicago v. FPC*, 458 F.2d 731, 734-37 (D.C. Cir. 1971) *cert. denied*, 405 U.S. 1074 (1972). *See generally Permian Basin Area Rate Cases*, 390 U.S. 747 (1968).

[14] *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738, *modified* 42 F.P.C. 1089(1969), *aff'd, City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972).

case of pipeline producers. In the face of dwindling gas supplies, the FPC indicated that its primary concern was to spur the development of new production. The FPC reasoned that the stimulus to additional production implicit in the area rates for producers should be directed toward increasing production by pipeline producers as well.[15] In its view, parity was essential to the creation of a "regulatory climate conducive to an aggressive pipeline exploration program."[16] Further, the FPC concluded that the use of the average ratemaking methodology could stimulate gas production by pipelines while protecting consumers from bearing the full cost of unsuccessful or inefficient ventures.[17]

Therefore, in Opinion No. 568, the FPC initiated a policy of parity of pricing treatment, under which gas produced by a pipeline or its affiliates from leases acquired after October 7, 1969, and taken into the pipeline's own system would be valued by reference to the just and reasonable area rates established for sales by independent producers in the same area. Those area rates would then be passed through the pipeline's purchased gas adjustment (PGA) clause.[18] Pipeline producers would be permitted to recover their production costs on a cost-of-service basis only upon showing that special circumstances existed which warranted such treatment.[19]

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[15] *Pipeline Production Area Rate Proceeding, supra* note 14, at 747.

[16] *Id.* at 745.

[17] *See City of Chicago v. FPC, supra* note 3, 458 F.2d at 738.

[18] 18 C.F.R. 2.66 (1979).

[19] 18 C.F.R. 2.66(a)(4). The FPC expressly stated that a pipeline's inability to recover its expenditures and earn the allowed return on production would not constitute special circumstances. *Pipeline Production Area Rate Proceeding*, Opinion No. 568-A, *supra* note 14, 42 F.P.C. at 1091; *See Kansas-Nebraska Natural Gas Company*, 53 F.P.C. 1691; 1696-1699 (1975).

The FPC continued this policy of parity in the nationwide rate proceedings, extending the nationwide rates to various vintages of pipeline production.[20] In Opinion No. 699-H, the FPC reaffirmed its decision that pipeline production flowing from pre-October 8, 1969, leases should continue to be priced on a cost-of-service basis, but concluded that pipeline production from wells drilled on or after January 1, 1973, should be valued at nationwide rates regardless of the date the lease was acquired.[21] Therefore, on the date of enactment of the NGPA, area or nationwide rates were applicable to all but two categories of pipeline produced gas: most production from pre-1973 wells on pre-October 8, 1969 leases, and production from other leases which had been granted cost-of-services treatment upon a showing of special circumstances or pursuant to a settlement in lieu of a finding of special circumstances.

III. Discussion: Parity of Pricing for Pipeline Production in the Context of the NGPA.

The enactment of Title I of the NGPA ended the prevailing system of domestic wellhead price regulation under which the Commission set rates for producer sales of natural gas to the interstate market, and the states regulated producer sales to intrastate markets. In its stead, Congress established a unified pricing scheme imposing maximum lawful prices for first sales by producers of domestically produced natural gas. The elimination of the dual market and the statutorily embraced commitment to price

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[20]*See* Opinion No. 770-A, *mimeo* at 147 (issued November 5, 1976) 56 F.P.C. 2698 (1976); Opinion No. 749-C, *mimeo* at 29 (issued July 19, 1976), *to be published at* 56 F.P.C. 303 (1976); Opinion No. 699-H, *mimeo* at 47 (issued December 4, 1974), *to be published at* 52 F.P.C. 1604, 1634-35 (1974).

[21]Opinion No. 699-H, *mimeo* at 47-50.

incentives are the cornerstones of the Congressional plan to encourage maximum production of natural gas.

However, the NGPA left substantially intact the Commission's authority under the NGA to regulate the rates and services of pipelines delivering gas in interstate commerce. The Congress left to the Commission the task of harmonizing its statutory mandate to implement the NGPA pricing scheme with its continuing authority under the NGA to determine the price treatment of natural gas produced by interstate pipelines and sold in mixed volume sales. Therefore, our goal in establishing a pricing scheme for pipeline production is to properly employ our regulatory tools under the NGA to coordinate the purposes of that Act with the policies established by the NGPA.

As we stated in the Notice of Proposed Rulemaking, the objectives which prompted the FPC to extend pricing parity to pipeline producers, to provide for equitable treatment among producers and to encourage additional exploration for the production of natural gas, remain desirable in the face of a transcendant public need for additional domestically produced energy supplies. In reliance on the FPC's policy, pipelines have competed for leases with independent producers and have undertaken substantial drilling programs which have produced increased gas supplies. As commenters point out, the aims of equity and regulatory stability are well served by a continuation of this parity policy.[22]

However, the role of parity pricing has been enlarged by the passage of NPGA and, in the context of our efforts to coordinate the NGA with the regulatory scheme of the NGPA, the arguments for parity treatment emerge as even more compelling. Prior to the NGPA, the FPC and the Commission recognized the need to offer price incentives to producers to encourage exploration and development of

[22]*See* comments of El Paso and Northern.

additional natural gas supplies.[23] Thus, the area and nationwide rates were designed to provide for recovery of the average costs of finding, developing and producing natural gas plus an incentive to compensate for the risks associated with lease acquisition, exploration and development. The Congressional decision to reorder the economic regulation of natural gas prices to provide a uniform system of statutorily prescribed incentives was based on a similar belief that such incentives are necessary to secure continued development and additional production of natural gas.

Having embarked under the NGA upon a course which would provide price incentives for both pipeline and independent producer production to encourage production of additional gas supplies, and having been reaffirmed in this course by evidence of a similar purpose in Congress' enactment of a pricing scheme in the NGPA designed to encourage additional production, we believe that our mandate of coordinating the NGPA and the NPA would best be accomplished through a policy of pricing parity among independent and pipeline producers. First, as many commenters point out, pipeline producers undertaking new exploration efforts must compete with independent producers may be willing to pay for leases will be influenced by the expected revenues for gas from the project, which will be priced at applicable Title I prices. If pipeline producers were held to pre-NGPA prices, or were subject ro a newly established cost-based nationwide rate, they would in many instances be unable to compete with independent producers in acquiring new leases. The resulting disincentive to pipeline production would deny the pipeline customers a more certain stream of additional supplies.

Further, the institution of a nationwide rate proceeding in order to account for changes in costs or market

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[23]*See Mobile Oil Corp. v. FPC*, 417 U.S. 283, 316-317 (1973); *Permian Basin Area Rate Cases*, 390 U.S. 747, 796-798 (1973).

conditions since 1975 might not cure the distortions created by disparate pricing treatment. If the cost-related incentive prices established in a nationwide ratemaking were less than the NGPA prices, pipelines would still be a competitive disadvantage in acquiring new leases. To the extent that the resulting nationwide rates varied in any respect from the NGPA rates, we would have established inconsistent schemes of wellhead price regulation, reincarnating the regulatory anomaly which Congress sought to eliminate in its enactment of Title I. Such an undertaking would effectively ignore the Congressional evaluation of price incentives, and would be, in our view, an insular and administratively wasteful endeavor. For these reasons we believe that the existing policy of parity of treatment for pipeline producers should be continued in the context of the NGPA.

The foregoing analysis demonstrating our reasons for extending pricing parity to pipeline producers previously subject to area or nationwide rates does not apply in the case of pipelines receiving cost-of-service treatment for production. In the case of gas yet to be produced from pre-1973 wells on pre-October 8, 1969 leases, we find little to persuade us that costs of production will not be recouped by the pipeline on a cost-of-service basis. As one commenter articulates the pertinent consideration:

> The pipeline's customers have paid [through the pipeline's rates] for the development and production costs, including components for return, income taxes, depreciation. As a result, the equity and incentive reasons for granting parity do not apply to such gas.[24]

As several commenters argue, the same consideration persuades us that parity should not be extended to pipeline producers subject to cost-of-services treatment under the special circumstances provisions of §2.66(a)(4).[25] Pipelines

[24]Comments of El Paso. *See* discussion *infra*.

[25]*See* comments of El Paso, Northern and New York.

receiving such treatment have enjoyed the advantage of passing on to their customers the risks of the pipeline's production ventures. Pipelines have passed on the costs of acquiring leases and the costs of exploration and development, including dry hole costs and other costs associated with unsuccessful and marginally successful ventures, in exchange for assuring their customers the opportunity to enjoy the additional volumes resulting from successful ventures at a price determined on a cost-of-service basis. The Commission therefore will not extend pricing parity to pipeline production which prior to the enactment of the NBPA was valued on a cost-of-service basis rather than by reference to area or nationwide area.

For the foregoing reasons, we are promulgating a final substantive rule[26] which continues the policy of parity of pricing treatment for pipeline production now subject to area or nationwide rates.

IV. Summary of Comments and Analysis of the Final Rule.

A. Parity of Price Treatment

In response to the Notice of Proposed Rulemaking, the American Gas Association (AGA), Natural Gas Pipeline Company of America (Natural), Consolidated Gas Supply Corporation (Consolidated), Northwest Pipeline Corporation (Northwest), Public Service Commission of the State of New York (New York), El Paso Natural Gas Company (El Paso), Southern Natural Gas Company (Southern), Northern Natural Gas Company (Northern), and United Gas Pipeline Company (United) have submitted comments expressing support for the parity policy. They commend the proposed rule as a logical extension of past

[26]The Notice of Proposed Rulemaking set out proposed §2.66a as a statement of policy, but indicated that the Commission might choose to issue these provisions as substantive regulations. Proposed §2.66a has been modified to reflect our decision that this policy should take effect as a substantive rule, which is promulgated at 18 C.F.R. §154.42.

Commission policy favoring parity of pricing treatment between pipelines and other producers in order to promote equity and fundamental fairness, and to encourage natural gas production. These commenters emphasize that absent parity of treatment, pipeline producers will be unable to compete for leases and develop new gas supplies for their customers.

Two comments raise various legal and policy objections to the concept of pricing parity. Kentucky-West Virginia Gas Company (Kentucky-West Virginia) argues that the establishment of pricing parity under the NGA is outside the scope of the Commission's authority, because it rests upon an improper interpretation of the NGPA's definition of first sale. It contends that any sale that includes volumes of pipeline production, including a mixed volume sale, is statutorily entitled to NGPA first sale treatment for any portion of the sale that is attributable to the pipeline's own production. Therefore, Kentucky-West Virginia argues, all pipeline production should be priced under the NGPA regardless of its prior treatment under the NGA.

Questions concerning the Commission's interpretation of the NGPA's first sale definition as it applies to pipeline production pertain directly to Order No. 58, and not to this rulemaking.[27] Therefore, we will deal with these comments when we consider applications for rehearing of Order No. 58.

The Kansas Corporation Commission (Kansas) objects to the policy underlying this rulemaking on wholly different grounds. In its view, the Commission has correctly interpreted section 2(21)(B) of the NGPA to exclude a pipeline's mixed volume sales from first sale treatment. However, it contends that the fact that such sales have been statutorily excluded from first sale treatment is evidence of

[27]Kentucky-West Virginia has articulated the same arguments in its application for rehearing of Order No. 58.

Congressional intent to prevent pipeline producers from collecting NGPA rates.

Kansas further argues that the Commission lacks authority to provide for the collection of NGPA rates under the NGA. It contends that a just and reasonable rate within the meaning of the NGA must be cost-based. In Kansas' view, the NGPA rates were established primarily to escape the bounds of the NGA's restrictive standards, necessarily implying that the NGPA rates are not just and reasonable. Finally, Kansas also contends that even if the Title I prices were just and reasonable, the Commission should not permit such rates to be collected for flowing gas and gas produced from properties acquired before enactment of the NGPA. Kansas argues that the allowance of an incentive price for such gas will not result in increased exploration and development activities, and therefore urges the Commission to offer NGPA incentive prices only for gas produced from leases acquired by a pipeline on or after November 9, 1978, where qualification for sections 102, 103, 107 or 108 has been obtained.

We cannot agree that our action is impermissible under the NGPA or the NGA. Our interpretation of the NGPA's first sale definition does not reflect the view that Congress intended to insure that pipeline production would be valued at a rate lower than that applicable to sales by independent producers. Rather, our interpretation of section 2(21)(B) is premised on the view that Congress chose to maintain NGA price regulation of mixed volume sales to facilitate the coordination of our on-going authority over pipeline services with our duties to implement the wellhead pricing scheme of Title I.[28] We find no evidence either in the legislative history or implicit in the language of section 2(21)(B) that Congress intended us to take no cognizance of the NGPA prices in exercising our pricing authority under the NGA.

The Commission is aware, of course, that rates granted under the NGA generally must be just and reasonable. We

[28] *See* Order No. 58, *mimeo* at 5-7.

do not believe, however, that our decision to permit pipelines to collect incentive rates commensurate with the NGPA prices works an unjust and unreasonable result.[29]

While it is true that the Commission's historical reliance on cost-based ratemaking methodology has nurtured the growth of an intricate regulatory scheme which has been, to a large extent, analytically dependent upon cost concepts, we have also consistently recognized that the rigors of a wholly cost-based methodology cannot accommodate the need for price incentives to induce the exploration for and development of additional gas supplies. In reviewing our policies in this regard the courts have indicated that although the Commission must consider cost factors in order to protect consumers from excessive rates, it may also include price incentive factors in the rate in order to assure consumers an adequate supply of gas.[30]

Although the Commission has employed several methodologies for pricing pipeline production, it expressed a preference for valuing pipeline production by reference to producer rates, because that method achieves parity of treatment and results in the least potential for

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[29]The Commission has broad authority in selecting methods for determining individual components of a pipeline's cost of service, so long as the resulting pipeline rate is just and reasonable under sectins 4 and 5 of the NGA. In *Hope Natural Gas Co. v. FPC*, 320 U.S. 591 (1943), the Supreme Court stated that a challenge to a Commission ratemaking decision involves the question "whether that order, 'viewed in its entirety' meets the requirement of the Act . . . It is the result reached not the method employed which is controlling." *Id.* at 602. We believe, however, that the Commission exercises its discretion in a manner most consistent with the provisions of sections 4 and 5 of the NGA when its values the pipeline production component of the pipeline's cost-of-service as well as the entire rate at levels which are just and reasonable within the meaning of the NGA.

[30]*See, e.g., American Public Gas Ass'n v. FERC*, 567 F.2d 1016, 1059 (1977), *cert. denied* 435 U.S. 907 (1978); *City of Chicago v. FPC, supra note* 13, 458 F.2d at 750-51 (D.C. Cir. 1971); *See also* note 23 *supra*, and accompanying text.

producer rates, because that method achieves parity of treatment and results in the least potential for distortion of the incentives and disincentives which govern investment decisions concerning natural gas production. Comments received in this docket and in the course of our consideration of Order No. 58 persuade us that failure to continue parity of treatment would introduce distortions into natural gas production investment decisions in derogation of the substantial public need for stable, domestically produced energy supplies.

Continuing this policy of pricing parity requires that we now price pipeline production by reference to NGPA prices. In doing so without instituting another nationwide ratemaking proceeding we have relied on Congress' conclusion that the NGPA prices reflect the composite of cost-based and non-cost-based factors necessary to encourage production of additional gas supplies. Based on this premise, we believe that the valuation of pipeline production by reference to NGPA rates represents the most reasonable reconciliation of consumer and producer interests, and therefore achieves a just and reasonable result.[31]

B. **Applicability of §154.42**[32]

The final rule in §154.42 implements the Commission's

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[31]Similarly, we believe that it is necessary under the NGA to require customers of interstate pipelines to bear the burden of certain non-cost incentives in order to assure that their needs for additional gas supplies are satisfied. The Commission has in the past granted higher prices for flowing gas, reasoning that a pipeline's customers should be required to share with future customers the higher costs of developing the natural gas supplies to replace the supplies they consume. Opinion No. 749, 54 F.P.C. 3090 (1975) *aff'd. Tenneco Oil Co. v. FERC*, 571 F.2d 834 (1976), *cert. dismissed*, 439 U.S. 801 (1978).

[32]The rule in this docket was originally proposed as a statement of policy and thus was drafted to amend Part 2 of the Commission's regulations, "General Policy and Interpretation" by creating a new §2.66a. Because we have decided to issue a substantive rule in this docket, we will amend Part 154, "Regulations Under the Natural Gas

decisions in this regard and, although it is being promulgated as a substantive rule rather than a statement of policy, is essentially the same as the rule set forth in the Notice of Proposed Rulemaking. It applies NGPA pricing to all non-first sale natural gas produced by an interstate pipeline or its affiliate on or after November 15, 1979 (the day after issuance of the Notice of Proposed Rulemaking) unless such production is from a lease acquired before November 15, 1979, that has ever been granted cost-of-service treatment. However, under new §154.42(a)(2), a pipeline would be able to obtain NGPA pricing for gas produced as early as December 1, 1978, provided it had either made a filing under section 4 of the NGA to collect the rate and the Commission's suspension of the rate was conditioned on the provisions of the final rules promulgated in this order, or it had filed for cost-of-service treatment under §2.66(a)(4) and such treatment was denied by the Commission after December 1, 1978.[33]

In commenting on the proposed rule, Columbia and Northern maintain that the Commission should allow pipelines to collect NGPA prices for all production after December 1, 1978, unless the Commission has provided otherwise by order. Northern argues that the Commission should not rely on the "procedural happenstance of whether the pipeline, either by suspension of a portion of its PGA adjustment filing or otherwise, has had its entitlement to rates conditioned on the provisions of the rule issued in this docket."

We do not agree that the effect of this provision is to condition a pipeline's rights upon "procedural happenstance." Pipelines who filed to collect Title I prices upon enactment of the NGPA were subject to the Commission's PGA regulations. At that time, §154.38

Act" to create a new §154.42, "Pricing of Certain Gas Produced on or after December 1, 1978, by Pipelines and Pipeline Affiliates."

[33]The provision for gas denied cost-of-service treatment is an addition to the rule as originally proposed. *See infra* note 44, and accompanying text.

authorized the passthrough of area or nationwide rates for pipeline production "that qualifies for and is being afforded area or nationwide rate treatment or is otherwise being afforded area or nationwide rate treatment as though the gas were being produced by an independent producer."[34] This limitation on a pipeline's ability to reflect its own production in a PGA filing was imposed in recognition of the fact that pipeline production priced on a cost-of-service basis was already being reflected in the pipeline's section 4 rates on a test period basis. In accordance with this provision, the Commission rejected any rate filing to collect NGPA prices for pipeline production subject to cost-of-service treatment as inconsistent with the provisions of the Commission's PGA regulations. The Commission suspended other filings where the pipeline had valued its own production, which was eligible for inclusion in its PGA, at NGPA rates and conditioned these filings on the outcome of this rulemaking. In this respect, the provisions of new §154.42(a)(2) are consistent with the policy reflected in §154.38 and affirmed in this rulemaking to exclude from parity pricing all pipeline production now subject to cost-of-service treatment.

With regard to pipeline production for which NGPA rate treatment is available, this provision is also consistent with the provisions of section 4 of the NGA and §154.38 which require a pipeline to file for rate increases before passing through the costs of purchased gas and its own production. Compliance with the filed rate requirement assures the Commission the opportunity to review the rates to determine whether they are eligible to be passed through to the pipeline's customers. The requirement to which Columbia and Northern object implements the Commission's intent, consistent with prior practice, to permit pipeline producers eligible for NGPA rates under the provisions of this rule to receive those rates from the effective date of the NGPA, if they have properly filed to

[34] 18 C.F.R. §154.38, n. 1 (1979).

collect them. For these reasons the requirement will be retained.

C. **Termination of Special Circumstances**

Because new §154.42 by its terms applies to all gas produced from leases acquired on or after November 15, 1979, that section would terminate prospectively relief based on special circumstances, since §154.42 does not contain a special circumstances provision similar to that in §2.66(a)(4).[35] One commenter urges the Commission to use its authority under section 502(c) of the NGPA to permit a pipeline to seek cost-of-service pricing treatment for its own production based upon a showing that collection of the applicable NGPA ceiling price works a special hardship upon the pipeline producer. Presumably such a provision would serve the same function as §2.66(a)(4).

First, the Commission emphasizes that, while section 502(c) empowers the Commission to make adjustments of its rules under the NGPA, the rules governing interstate pipeline production are promulgated under the NGA, and thus technically are not subject to adjustment under section 502(c). Furthermore, the Commission has determined that the NGPA prices provide a system of incentives which adequately compensates a pipeline producer for the risks associated with exploration and development. We therefore decline to extend cost-of-service treatment to pipeline producers not currently on cost-of-service. However, in the Notice of Proposed Rulemaking, the Commission indicated that special relief would be available to pipeline producers to the same extent that it is available to independent producers to encourage investment in new production projects and production enhancement work, and to cover operating and maintenance expenses that cannot be recouped under the applicable NGPA rates.

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[35]The termination of the special circumstances provision has no retroactive effect. Pipeline production from leases which have ever been subject to cost-of-service treatment will continue to be subject to such treatment. *See* discussion *infra*.

The Commission is presently considering regulations governing applications for special relief applicable to independent producers and pipeline producers whose sales qualify as first sales under §270.203[36], and has specifically solicited comments discussing whether the proposed provisions for special relief should be made available to pipeline producers for gas not sold in first sales. That issue will be resolved within the context of the special relief rulemaking.

D. **Requirements to Collect NGPA Rates**

Section 2.66a(b)(1)(i)[37] of the proposed rule set out the general policy permitting pipelines to value their production that is subject to §2.66a by reference to Title I prices prescribed under Subparts B, C, D, G, H or J, and under Subpart K of the Commission's regulations, if certain conditions are met.

In the Notice of Proposed Rulemaking we did not raise directly the question whether pipeline producers should be permitted to collect deregulated prices if the sale is not a first sale. However, in the interim rulemaking deregulating the price of natural gas subject to section 107(c)(1)-(4), the Commission requested comments on whether production by interstate pipelines should be valued by reference to the price of natural gas deregulated under the NGPA. All of the comments addressing this issue urge the Commission to extend such rates to eligible pipeline producers.

We recognize that in deregulating high-cost gas, Congress determined that the production of such gas should be encouraged at whatever price the market will bear. We believe that the same incentive price should be available to interstate pipelines and have therefore modified the proposed rule to permit interstate pipelines to value

[36] Notice of Proposed Rulemaking, Procedures Governing Applications for Special Relief under sections 104, 106 and 109 of the NGPA, Docket No. RM79-67 (issued June 9, 1980).

[37] *See* §154.42(b)(1) of the final rule.

their production of such high cost gas by reference to our rules in Part 272 concerning deregulation.

The Commission is concerned, however, that reference to a market price imposes no meaningful limitation on the pipeline's valuation of its own production, which is not determined by contract negotiation.[38] Section 601(b)(1)(E) of the NGPA addresses the problem created by the absence of a true bargaining relationship when a first sale contract price is established by an interstate pipeline and its producing affiliate regarding regulated as well as deregulated gas. That section provides that the price paid in the first sale by a pipeline to its affiliated producer will not be deemed just and reasonable (and therefore will not be subject to PGA passthrough) unless the price does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.

In order to accomplish a similar purpose for pipeline producers, §2.66a(b)(1)(ii)(A)[39] of the proposed rule conditioned the availability of price parity treatment on compliance with the affiliated entities rule in section 601(b)(1)(E). Such a requirement would impose a market based limitation on the valuation of all pipeline production, including deregulated gas, comparable to contract price limitations borne by independent producers.

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[38]Kansas claims that proposed §2.66a created "super parity" because it allows pipelines NGPA prices while NGPA prices available to producers are limited by contract. Kansas states that this will be used to the advantage of producers in Order No. 23-B protest proceedings. Acknowledging, as Kansas does, that all producers contracts after December 1, 1978, will have rate clauses referencing Congressionally set rates, so in that regard there is no "super parity" as to pre-December 1, 1978 contracts, the "affiliated entities limitation" in proposed §2.66a(b)(1)(ii)(A) and in new §154.42(b)(1) prevents pipelines from costing their own production on the basis of NGPA rates where that pipeline or other pipelines are paying less than NGPA rates to other producers.

[39]*See* §154.42(b)(1) of the final rule.

The Commission remains persuaded that pipeline producers who receive parity of pricing treatment should be subject to a market based limitation on the valuation of their own production. However, the proposed regulation's reference to the affiliated entities rule of section 601(b)(1)(E) may be inadequate because the language of section 601(b)(1)(E) is, on its face, applicable only to first sales between interstate pipelines and their affiliates. For this reason, we have modified the language of the proposed rule to make it clear that pipeline production may not be valued at a rate in excess of the amount paid in comparable sales between persons not affiliated with the interstate pipeline or with each other. The modification has been incorporated into the general rule regarding NGPA pricing treatment in new §154.42(b)(1). Under that provision qualifying production as defined in paragraph (b)(2) is priced at the lower of the applicable NGPA referenced rate or the amount paid in comparable sales between persons not affiliated with the pipeline or with each other.

Section 2.66a(b)(1)(ii) of the proposed rule contained two other conditions with which a pipeline was required to comply before receiving NGPA rates for its production. The pipeline was required to comply with all of the requirements in Subchapter H, including those relating to filing requirements for jurisdictional agency determinations, provisions for interim and retroactive collection, and Part 276 reporting requirements. The requirement that a pipeline or affiliate comply with the requirements of Subchapter H, except the requirement of §270.101(d)(1), has been retained in §154.42(b)(3) of the final rule. We are aware, however, that pipelines may have been uncertain as to their filing obligations with regard to production not sold in a first sale, and may have failed to make timely filings as required under Subchapter H. We have therefore provided in new §154.42(b)(3)(i) that a pipeline may be granted a waiver of any time of filing

requirement upon showing that a timely filing was not made because the pipeline had no notice that it was subject to such requirement.[40]

In addition, the proposed rule conditioned a pipeline's authority to collect the applicable NGPA rates upon compliance with the rate change filing requirements applicable to independent producers under §154.94 of the Commission's regulations. Section 154.94 establishes blanket affidavit filing requirements which permit a qualifying producer who filed a blanket affidavit prior to December 30, 1978, to collect NGPA prices retroactively to December 1, 1978, the effective date of the NGPA. Under §154.94 producers who file on or after December 30 may only collect NGPA prices prospectively. Southern and Sonat request that the Commission modify this restriction, pointing out that pipeline producers had no notice that such requirements could be applicable to them and therefore complied only with the PGA rate change requirements in §154.38.

After reviewing the requirements of §154.94, we have concluded that they impose unwarranted burdens on pipeline producers. We now believe that it is adequate for pipeline producers to report the value of their own production through their PGA filings, which in the past have provided the Commission with adequate information regarding the validity of such charges. Therefore, the Commission has provided in §154.42(b)(3) that a pipeline need not comply with §270.101(d)(1) of Subchapter H which require compliance with the filing requirements set out in §§154.92 and 154.94.

E. Exception for Natural Gas Subject to Cost-of-Service Treatment

As noted above, the proposed rule excluded from

[40]This provision for waiver of filing requirements does not extend to waiver of applicable PGA filing requirements under 18 C.F.R. §154.38.

eligibility for NGPA referenced rates any pipeline production which has ever been subject to cost-of-service treatment. Under proposed §2.66a(b)(1)(i),[41] production from pre-1973 wells on pre-October 8, 1969 leases remained subject to cost-of-service rate treatment. Also, under §2.66a(b)(1)(iii) and (b)(2), the Commission proposed to continue cost-of-service treatment for any gas granted such treatment under the special circumstances provisions of §2.66(a)(4).

El Paso, New York, and Northern strongly support the exclusion of cost-of-service gas from parity treatment, arguing that in these cases the pipeline's stockholders have not borne the risk of exploration and production (as in the case of production valued at area or nationwide rates), and thus the pipelines do not need the price incentives for such gas.

Although CIG and Columbia also agree with the Commission's proposal to extend NGPA prices to pipeline production which is not subject to first sale treatment, they argue that the Commission should provide complete parity for pipeline production by allowing all pipeline production to be valued by reference to NGPA prices. They maintain that such a rule furthers the purposes of the NGPA to provide capital and other inducements to explore for and develop additional gas, and "to promote conservation of a finite and strategic substance by causing the consumers to pay a price more representative of its replacement cost."

CIG also argues that whether pipeline production gets cost-of-service treatment or the section 104 rate, those prices should be escalated monthly by the statutorily prescribed inflation factor, because Congress intended the rate for all production under the NGPA to escalate for inflation. Finally, CIG argues that pipelines need the same incentives provided under section 108 for stripper wells as other producers will receive. CIG maintains that cost-of-

[41] *See* §154.42(b)(2)(i)(A)-(D) of the final rule.

service treatment does not provide sufficient incentives since old wells have already been depreciated and thus, the rate of return allowed under cost-of-service treatment would produce a rate lower than the section 108 maximum lawful price.

As discussed above, the Commission believes that there are compelling reasons for not allowing cost-of-service production gas have provided the pipeline with significant cost guarantees and other benefits not available to indepedent producers. The Commission agrees with El Paso, Northern, and New York that retaining cost-of-service treatment for production granted cost-of-service treatment under special circumstances provides all parties concerned with what they bargained for. We also note that cost-of-service treatment, in permitting the recovery of test period costs, provides for recovery of increased costs due to inflation. Therefore, the NGPA inflation adjustment is not necessary to assure these pipelines the full recovery of their costs. For these reasons, the Commission declines to modify new §154.42 to extend NGPA rates to all pipeline production.

Several comments request that the Commission clarify the effect on certain particular cases of the language of the exclusion in what is now §154.42(b)(2)(iii) concerning leases acquired before November 15, 1979 which have ever been granted cost-of-service treatment upon a showing of special circumstances. New York argues that by limiting the scope of the exclusion to gas produced from leases *granted* cost-of-service treatment, the Commission has failed to make clear the treatment to be accorded pipeline production valued on a cost-of-service basis as a result of a settlement, or pending final disposition of a special circumstances application. New York urges the Commission to require, in both types of cases, that such production continue to be valued on a cost-of-service basis, arguing that pipelines that have enjoyed the benefits of cost-of-service treatment should not now be permitted to collect the higher NGPA rates.

New York correctly notes that in many cases pipeline production has been subject to cost-of-service treatment pursuant to a settlement agreement adopted in lieu of a Commission finding of special circumstances. It was our intent in §2.66a(b)(1)(iii) of the proposed rule that such treatment continue in effect. We have therefore provided more clearly for that result in new §154.42(b)(2)(ii) by expressly excepting from NGPA treatment natural gas from leases which have ever been granted cost-of-service treatment pursuant to a settlement approved in lieu of a finding of special circumstances.

The Commission addressed the issue of pending proceedings in the Notice of Proposed Rulemaking, indicating that we would not use this rulemaking to dispose of the matters pending before the Commission in Docket No. RP75-106.[42] In that docket, Columbia Gas Transmission Company sought to show that special circumstances existed which warranted cost-of-service treatment for certain of Columbia's Appalachian production. Since the issuance of the Notice of Proposed Rulemaking, the Commission in Opinion No. 74 has determined that special circumstances do not exist and has therefore denied Columbia's request for cost-of-service treatment.[43] Therefore, because Columbia has not been

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[42]Notice of Proposed Rulemaking, *supra* note 19, at 11 n. 7. Also in the Notice, the Commission noted that Michigan-Wisconsin Pipeline Company received cost-of-service treatment uner §2.66(a)(4) for the period November 1, 1973 through October 31, 1977, but that the Commission in approving settlements covering rates for subsequent periods "has expressly disavowed any policy decision regarding the pricing approach incorporated in the settlements." *Id.*

[43]On June 27, 1980, the Commission voted to deny rehearing of Opinion No. 74.

granted cost-of-service treatment under the special circumstances provisions of §2.66(a)(4), Columbia may value its production that it otherwise eligible under this rule by reference to NGPA maximum lawful prices.[44]

Northern has requested that the Commission modify the cost-of-service exemption with regard to production of gas from leases now subject to modified cost-of-service rate treatment. Under Northern's modified cost-of-service rate treatment, the pipeline values a portion of its production on a cost-of-service basis and the remaining portion by reference to area rates. Northern notes that in its case, the percentages are computed as an undivided rate and are not allocated among the pipeline's producing leases. Thus, it is concerned that all production from any lease subject to 75 percent cost-of-service treatment would be subject to cost-of-service treatment rather than NGPA referenced rates. They urge the Commission to amend §2.66a(b)(1)(iii) of the proposed rule[45] to exclude from parity of price treatment "production from leases acquired before November 15, 1979, to the extent such *production* has ever been granted cost-of-service treatment pursuant to §2.66a(a)(4) (relating the special circumstances.)" (emphasis added).

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[44]Section 154.42(a)(2)(ii) makes clear that pricing parity is applicable to all of Columbia's production since December 1, 1978, that has been denied cost-of-service treatment in Docket No. RP75-106. Columbia is nevertheless subject to other requirements of this rule and the Commission's regulations under the NGA. These include, but are not limited to, the filed rate doctrine of section 4 of the NGA and §§154.38 and 154.63 of the Commission's regulations, and the requirement under §154.42(b)(3)(i) that a pipeline comply with the provisions of subchapter H, absent a waiver.

[45]*See* §154.42(b)(2)(ii) of the final rule.

It was the Commission's intent in establishing this rule to leave intact existing pricing schemes which were designed to encourage the drilling programs of individual pipelines. Because we agree that pipelines subject to modified cost-of-service treatment should continue to value the designated percentage of their production by reference to prices applicable to sales by independent producers (NGPA rates), we have expressly provided for that result in new §154.42(b)(2)(ii).

El Paso urges the Commission to adopt a similar amendment to §2.66a(b)(1)(iii) of the proposed rule for somewhat different reasons. In El Paso's view, the Commission erred in applying the exclusion to natural gas from leases acquired before November 15, 1979, if any production from such leases was ever accorded cost-of-service treatment. El Paso contends that new production from such leases should receive parity treatment, and therefore urges the Commission to limit the language of new §154.42(b)(2)(ii) to exclude only that "production" which has never been granted cost-of-service treatment under special circumstances.

El Paso appears to have misconstrued the Commission's purpose in excluding cost-of-service gas from NGPA rate treatment. It was our design to enforce the perimeters which the pipelines themselves drew around their drilling programs. In determining the applicable cost-of-service allowance, the Commission included the pipeline's costs of lease acquisition, exploration and development. The risks associated with these expenditures have already been passed on to the pipeline's customers. We therefore will continue to treat on a cost-of-service basis any gas produced from developed or undeveloped leases, if such leases were acquired before November 15, 1979, and were ever subject to cost-of-service treatment.

F. Abandonment of Leases Now Subject to Cost-of-Service Treatment

In the Notice of Proposed Rulemaking, the Commission expressed its concern that pipelines may seek to circumvent the exclusion of cost-of-service gas from NGPA price treatment by spinning-off to affiliates their properties which are now valued on a cost-of-service basis. Under §270.203(c), the affiliate's sale back to the pipeline of gas from those properties would be a first sale. We emphasized that any such transfer would require the Commission's authorization of abandonment. Also, because the gas is committed or dedicated to interstate commerce within the meaning of section 2(18) of the NGPA, we took the position that the affiliate would be required to file a certificate application in order to make the sale of the transferred gas to the interstate pipeline. We cautioned pipelines that the Commission would closely scrutinize abandonment and certificate applications to assure that the transaction is not merely an attempt by the pipeline to avoid continued cost-of-service pricing treatment.

Kentucky-West Virginia objects to our statements in the Notice of Proposed Rulemaking that we would carefully scrutinize any attempt by a pipeline to transfer its leases to an affiliate in order to circumvent our decision to deny parity of pricing treatment to pipelines now subject to cost-of-service treatment. It maintains that any attempt by the Commission to deny a certificate to an affiliate of a pipeline in order to prevent the affiliate from selling production from leases transferred from the pipeline and then sold back to the pipeline at NGPA prices would be contrary to section 601(c) of the NGPA. Section 601(c) provides that the Commission cannot deny or condition the grant of any certificate under section 7 of the NGA based upon the amount paid in any sale if such amount is deemed

"just and reasonable" under section 601(b). Section 601(b) deems NGPA prices to be just and reasonable if paid in a first sale, subject to certain conditions.

The Commission does not believe that its authority under the NGA to scrutinize such a transaction has been significantly limited by the NGPA. Assuming that the interpretation of 601(c) proffered by Kentucky-West Virginia is correct, the pipeline is nevertheless required to obtain the Commission's authorization before it may transfer its production properties.[46] The Commission reiterates that we will closely scrutinize any attempt to spinoff developed and undeveloped leases and will exercise our full authority to prevent spin-offs undertaken in order to circumvent the policies established in this rule.

EFFECTIVE DATE

This final rule is effective [thirty days after date of issuance.]

(Natural Gas Policy Act of 1978, 15 U.S.C. 3301 *et seq.*; Natural Gas Act, as amended, 15 U.S.C. 717 *et seq.*; Department of Energy Organization Act, 42 U.S.C. 7107 *et seq.*; E.O. 12,009, 42 *Fed. Reg.* 46267.)

In consideration of the foregoing, the Commission amends Part 2 of Subchapter A, Part 154 of Subchapter E, and Part 270 of Subchapter H, Chaper I, Title 18, Code of Federal Regulations, effective [30 days from date of issuance.]

By the Commission.
(S E A L)

Kenneth F. Plumb,
Secretary.

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[46] *See*, Opinion No. 626, *Panhandle Eastern Pipe Line Co.*, 48 F.P.C. 518 (1972).

1. Part 2 is amended in the table of contents and in the text of the regulations by inserting in the title of §2.66 the word "certain" between "of" and "new" and is further revised by adding to the end of the text of §2.66 the following new paragraph:

(e) **Inapplicability to certain gas produced on or after December 1, 1978.** This section does not apply to natural gas produced on or after December 1, 1978:

(1) if such gas is sold in a first sale, as determined under §270.203 of this chapter; or

(2) if §154.42 is applicable to such gas.

2. Part 154 is amended in the table of contents and in the text of the regulations by adding after §154.41 the following new §154.42:

§154.42. **Pricing of certain gas produced on or after December 1, 1978, by pipelines and pipeline affiliates.**

(a) **Applicability.** This section applies to natural gas that is produced by an interstate pipeline or an affiliate thereof and that is delivered to such pipeline, other than in a first sale, if:

(1) such gas is produced on or after November 15, 1979; or

(2) such gas is produced on or after December 1, 1978, and before November 15, 1979, and

(i) is specifically made subject by Commission order to the outcome of the proceeding in which this section has been promulgated; or

(ii) such pipeline's or affiliate's filing for cost-of-service treatment for such gas was denied by the Commission under §2.66(a)(4) of this chapter after December 1, 1978, for failure to show special circumstances justifying such treatment.

(b) **NGPA rate treatment.**

(1) **General rule.** Natural gas to which this section applies and for which NGPA rate treatment is available under sub-paragraph (2) of this paragraph shall be priced for ratemaking purposes in any pipeline rate proceeding at the lower of:

(i) the rate that would have been applicable under Part 271 or under Part 272 of Subchapter H had the gas been delivered to the pipeline in a first sale; or

(ii) the amount paid in comparable sales (which may also be first sales) between persons not affiliated with such interstate pipeline or with each other.

(2) **Gas for which NGPA rate treatment is available.**

(i) For purposes of this section, NGPA rate treatment is available (except as provided in clause (ii)) for natural gas if the production is from a lease owned by a pipeline or affiliate thereof and if:

(A) the lease was acquired after October 7, 1969; or

(B) the natural gas is produced from a well commenced on or after January 1 1973; or

(C) the natural gas is produced through a well commenced prior to January 1, 1973, as a result of a completion operation commenced on or after such date into a different, formerly nonproductive reservoir; or

(D) the Commission, prior to December 1, 1978, had granted area or nationwide rate treatment for such gas in lieu of otherwise applicable cost-of-service treatment; except that NGPA rate treatment shall be available only for natural gas produced during the period for which area or nationwide rate treatment was provided in applicable Commission orders and shall also be subject to the conditions specified in such orders.

(ii) **Exclusion from NGPA rate treatment.** NGPA rate treatment is not available for natural gas produced from leases acquired before November 15, 1979, which have ever been granted cost-of-service treatment pursuant to §2.66(a)(4) of this chapter or pursuant to a settlement approved by the Commission in lieu of a finding of special circumstances under that section; except that in the case of natural gas from leases which have been granted area or nationwide rates for some specified percentage, NGPA rate treatment is available for that specified percentage.

(3) **Subchapter H requirements.** A pipeline or affilite that produced natural gas for which NGPA rate treatment is available under paragraph (2) shall be subject to all the requirements of Subchapter H that would have been applicable had the natural gas been delivered pursuant to a first sale other than the requirement of §270.101(d)(1) regarding applicable filing requirements under §154.92 and §154.94. Such pipeline or affiliate may apply for a waiver of any time-of-filing requirement in Subchapter H based on a showing that a timely filing was not made because such pipeline or affiliate had no notice that it was subject to such requirement under this subparagraph.

(c) **Cost-of-service treatment.** In any pipeline rate proceeding, natural gas to which this section applies and for which NGPA rate treatment is not available shall be priced for ratemaking purposes on a cost-of-service basis.

(d) **Definitions.** For purposes of this section:

(1) **NGPA definitions.** The terms "interstate pipeline," "affiliate," and "first sale" have the same meaning as they have for purposes of Subchapter H.

(2) **Lease.** The term "lease" includes any fee interest in producing property of any working interest in production.

(3) **Pipeline rate proceeding.** The term "pipeline rate proceeding" includes a proceeding under §154.38(d)(4).

3. Part 154 is further amended by deleting the first sentence in footnote 1 to §154.38(d)(4) and substituting the following sentence in lieu thereof:

[1]For the purpose of this paragraph, purchased gas costs represent the cost of wellhead purchases, field line purchases, plant outlet purchases, transmission line purchases, and pipeline or affiliate production that qualifies for and is being afforded an area or nationwide rate under §2.66 of this chapter, a maximum lawful price under §270.203 of this chapter, or a rate specified under §154.42(b)(1).

* * *

4. Part 270 is amended in §270.203 by adding a new paragraph (f) to read as follows:

(f) **Cross reference.** For treatment of interstate pipeline and affiliate production delivered to a pipeline other than in a first sale, see §2.66 and §154.42 of this chapter.

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Charles B. Curtis, *Chairman;* Georgiana Sheldon, Matthew Holden, Jr., and George R. Hall.

Final Rule Governing the Maximum Lawful Price for Pipeline, Distributor, or Affiliate Production	)))	Docket No. RM80-7
Pricing of Pipeline and Affiliate Production under the Natural Gas Act	))	Docket No. RM80-6

ORDER NO. 102

ORDER DENYING REHEARING OF ORDER NO. 58 AND ORDER NO. 98 AND CLARIFYING ORDER NO. 98

(Issued October 3, 1980)

I. Introduction.

A. First Sales Under the NGPA.

Before the enactment of the Natural Gas Policy Act of 1978 (NGPA), section 1(b) of the Natural Gas Act (NGA) granted jurisdiction to the Federal Energy Regulatory Commission (Commission) to establish rates for sales for resale of natural gas in interstate commerce. Natural gas companies whose sales were subject to Commission rate regulation under the NGA included independent and pipeline affiliated producers, which ordinarily produce natural gas for sale to interstate pipeline purchasers, and interstate pipelines, which transport for sale natural gas acquired from independent or affiliated producers, or produced by the pipeline itself. Jurisdiction to determine rates for producer and pipeline sales in interstate commerce was reserved to state and local authority.

The resultant disparity between prices for producer sales in the interstate and the intrastate markets, which tended to discourage dedication of new production to interstate commerce, compelled Congress to eliminate the jurisdictional barriers to a nationwide market. The NGPA supplants the Commission's jurisdiction to set rates for independent and pipeline-affiliated producer sales of natural gas, and draws certain intrastate producers' sales int the field of federal price regulation.[1] To stimulate production, Congress devised a system of maximum lawful prices for domestically produced natural gas, embodying the incentives that Congress found were necessary to induce investment in exploration for and development of new reserves.

The NGPA maximum lawful prices were uniformly applied to "first sales" of natural gas to the new nationwide market, which is comprised of interstate and intrastate pipelines, local distribution companies, and direct sale customers. To insure that natural gas would be delivered to the market at the NGPA prices, Congress also made the wellhead prices applicable to sales preceding sales to pipelines, distributors, and direct sale customers.[2]

However, the NGPA does not terminate the jurisdiction of the Commission to regulate the rates charged for

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[1] *See* discussion *infra* at page 16.

[2] Section 2(21)(A) of the NGPA defines "first sale" as "any sale of any volume of natural gas --

(i) to any interstate pipeline or intrastate pipeline;
(ii) to any local distribution company;
(iii) to any person for use by such person;
(iv) which precedes any sale described in clauses (i), (ii), or (iii); and
(v) which precedes or follows any sale described in clause (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of the maximum lawful price established under this Act.

transmission and sale of gas acquired and transported by interstate pipelines. Although the statute modifies that jurisdiction in certain respects in order to facilitate coordination of the Commission's responsibilities under the NGA and NGPA,[3] Congress left substantially intact the regulatory apparatus for determining just and reasonable rates applicable to sales of gas acquired and transported by interstate pipelines.

Congress recognized that pipelines and distributors, in addition to acquiring and transporting gas for sale, also engage in production activities. It drew a distinction between a pipeline or distributor's producer or field sales, and other sales that remain subject to Commission or state jurisdiction. Section 2(21)(B) of the NGPA provides that the term first sale

> "shall not include the sale or any volume of natural gas by any distribution company, or any affiliate thereof, unless the sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof."

In Order No. 58[4], the Commission promulgated §270.203 of its regulations, determining which sales of natural gas by a pipeline, local distribution company, or affiliate thereof are first sales within the meaning of section 2(21)(B) of the NGPA. Paragraph (a) of §270.203 provides that:

> "(f)or purposes of applying section 2(21)(B) of the NGPA, a sale by a pipeline or distributor is a sale

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[3]For example, section 601(c) facilitates interstate pipeline passthrough of the purchased gas cost of natural gas acquired in a first sale, by providing that a price no greater than the applicable maximum lawful price is deemed just and reasonable for purposes of determining a pipeline's cost-of-service under the NGA.

[4]Order No. 58, Final Rule Governing the Maximum Lawful Price for Pipelne, Distributor of Affiliate Production (Docket No. RM80-7, issued November 14, 1979), 43 Fed. Reg. 60577 (Nov. 20, 1979).

> of natural gas attributable to volumes of natural gas produced by such pipeline or distributor to the extent that such sale is comprised exclusively of production volumes of natural gas from identifiable wells, properties, or reservoirs which are owned by such pipeline or distributor."

This interpretation reflects the Commission's view that the purpose of section 2(21)(B) is to distinguish between pipeline and distributor sales occurring at the wellhead or in the field[5], and sales from a pipeline's or distributor's general system supply. Wellhead or field sales clearly are sales attributable to a pipeline's or distributor's own production; sales from a pipeline's system supply are comprised of commingled volumes of purchased gas and pipeline production. Thus, the volumes are attributable to the production properties of independent producers, producing affiliates of the pipeline, and the pipeline itself. This distinction between two types of pipeline and distributor sales, embodied in §270.203, is consistent with the language of section 2(21)(B), and with the legislative objective of coordinating the pricing scheme of Title I with the on-going jurisdiction of the Commission and state and local authorities to determine rates for sales of natural gas transported for sale by pipelines and distributors.[6]

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[5]Sale of natural gas by a pipeline or distributor would be a first sale if it were an off system sale, or if the pipeline committed volumes of gas from an identifiable well to a particular purchaser and subsequently withdrew equivalent volumes from system supply for sale to the purchaser. *Id., mimeo* at 4.

[6]Section 2(21)(A)(v) of the NGPA empowers that Commission to add to the statutory definition of first sale, in order to prevent circumvention of the NGPA maximum lawful prices. Therefore, certain mixed volume sales by pipeline and distributors could be denominated first sales and thus become subject to NGPA maximum lawful prices. In exercise of this authority, the Commission has provided in § 270.203(b) that in order to prevent circumvention of the maximum lawful prices

In contrast with a pipeline that engages directly in production activities, a producing affiliate of a pipeline or distributor that is not itself a pipeline or distributor does not sell mixed volumes of natural gas. Instead, like an independent producer, a producing affiliate sells its production volumes to its affiliated pipeline or distributor, or to other purchasers. Consistent with paragraph (a) of §270.203, §270.203(c) treats such sales as first sales within the meaning of section 2(21)(B), because the sales are comprised wholly of volumes attributable to the affiliate's own production.[7]

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established under Title I of the NGPA, the term "first sale" includes a mixed volume sale by a pipeline or distributor unless the price at which such natural gas is sold is regulated pursuant to the Natural Gas Act or is regulated by a State agency empowered by State statute to establish, modify or set aside the rate for such sale, or the Commission, on application, has determined not to treat such sale as a first sale. This rule preserves the existing division of state and federal authority over such sales, but asserts NGPA pricing jurisdiction over sales that are not subject to rate regulation in order to insure that NGPA prices will not be circumvented.

[7]Section 270.203(c) provides:

> (c) *Sales by certain affiliates.* Any sale by an affiliate of a pipeline or distributor is a first sale if such affiliate is not itself a pipeline or distributor, unless the Commission, on application, has determined not to treat such sale as a first sale. For purposes of this paragraph, the term "sale" does not include any transaction between an interstate pipeline and an affiliate thereof if such transaction would not have been treated as a sale for purposes of the Natural Gas Act.

This rule includes sales by non-producing affiliates that are not themselves pipelines or distributors, such as gatherers or other middlemen. Although sales by unaffiliated middlemen are first sales under Section 2(21)(A), *see supra* note 2 and accompanying text, sales by middlemen affiliated with pipelines or distributors are excluded from first sale treatment under section 2(21)(B). Because historically these sales largely are unregulated, the Commission, by use of its authority under section 2(21)(A)(v), has denominated these sales as first sales to avoid circumvention of the NGPA maximum lawful prices.

B. **Pricing of Interstate Pipeline Production Under the NGA.**

If a sale by a pipeline of its own production is not a first sale, the applicable rate is determined by the Commission pursuant to its authority under the NGA. In determining interstate pipeline rates under the NGA, the Commission values the pipeline's production volumes sold in a mixed volume sale as a component of the pipeline's cost-of-service. Prior to the NGPA, the Commission had sought to provide parity of pricing treatment among independent and interstate pipeline producers by permitting a pipeline to value its production by reference to the area or nationwide rate that would have been applicable to the gas if it had been produced by an independent producer.[8] Area or nationwide rates were made applicable to natural gas produced from wells drilled after January 1, 1973, on leases acquired before October 8, 1969, and from all wells drilled on leases acquired after October 7, 1969.[9] Production from other, older wells, drilled prior to the institution of the parity pricing policy, continued to be valued on a cost-of-service basis.[10]

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[8]18 C.F.R. § 2.66. *See* Opinion No. 568, *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738, *modified* 42 F.P.C. 1089 (1969), *aff'd. City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972); Opinion No. 699-H, *mimeo* at 47-50 (issued December 4, 1974), *to be published* at 52 F.P.C. 1604, 1634-35 (1974).

[9]Although the pipeline production was not acquired in a sale and no certificates were issued for the pipeline's acquisition of its own production, the Commission allowed the value for such gas, determined by reference to area or nationwide rates, to be reflected in the pipeline's semi-annual purchased gas filings and passed through to purchasers on the same basis as natural gas purchased from producers. 18 C.F.R. § 154.38(d)(4), note 1.

[10]The costs of pipeline production subject to cost-of-service treatment, along with the pipeline's other costs, is reflected in the piepline's rate filings under section 4 of the NGA.

Also, a pipeline whose production was made subject to parity pricing treatment was permitted an opportunity to demonstrate that special circumstances existed that warranted exemption from area or nationwide rate treatment; a pipeline that demo rated such special circumstances was permitted to value its production on a cost-of-service basis.[11] In addition, the Commission approved settlements in rate proceedings providing some for of cost-of-service treatment for certain pipelines that failed to demonstrate special circumstances, but that had demonstrated that to some extent cost-of-service treatment was necessary to encourage their expanded production programs.[12]

In Order No.98[13], the Commission re-examined its pricing parity policy in light of the enactment of the NGPA. The Commission found that the incentive prices established by Congress under the NGPA should be used to encourage interstate pipelines to develop additional supplies of natural gas.[14] It therefore promulgated §154.42 of it regulations, which permits pipelines that were previously subject to area or nationwide rate treatment to value their production, for purposes of PGA passthrough, by reference to the NGPA price that would have been applicable to the gas if it had been sold in a first sale. However, the Commission found that such incentive prices should not be available for production from leases previosly subject to cost-of-service treatment, reasoning that such pipelines have already enjoyed the benefits of a certain recovery of and return on the costs of production, and that their customers, who have borne the risks of this investment

[11]18 C.F.R. § 2.66(a)(4)(1980).

[12]S*ee, e.g.*, Kansas-Nebraska Natural Gas Company, Inc., Docket No.s RP72-32, RP74-11, RP76-8 (issued December 7, 1976).

[13]Order No. 98, Final Rule Governing Pricing of Pipeline and Affiliate Production under the Natural Gas Act (Docket No. RM80-6, issued August 4, 1980), 45 Fed. Reg. 53091 (Aug. 11, 1980).

[14]*Id., mimeo* at 10-15.

in the early years of exploration and development, should have an opportunity to receive the price benefits of cost-of-service treatment for gas produced as a result of the expenditures.

C. **Applications for Rehearing.**

The Commission has received five timely applications for rehearing of Order No. 58,[15] arguing that the definition of

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[15]Timely applications were filed by the Mid-Louisiana Gas Company (Mid-louisiana), Kansas-Nebraska Natural Gas Company, Inc. (Kansas-Nebraska), Michigan Wisconsin Pipe Line Company (Michigan-Wisconsin), Consolidated Gas Supply Corporation (Consolidated) and Kentucky-West Virginia Natural Gas Company (Kentucky-West Virginia).

The Wallace Energy Corporation (Wallace) filed application for rehearing 31 days after the issuance of Order No. 58, has moved that the Commission deem the application timely filed, and has moved for a stay in the effectiveness of the rule as it applies to Wallace. We express no view on Wallace's argument that the Commission is obliged to deem its application timely filed. However, recognizing that its application was filed only one day after the closing of the period for rehearing, the Commission will treat the application as a motion for reconsideration and consider the merits of Wallace's arguments in this Order. Wallace is pursuing issues on Rehearing of Order No. 58 in two other forums before the Commission, and has now been granted interim relief by the Director of Office of Pipeline and Producer Regulation. *See*, Order of the Director, OPPR, Granting Interim Relief (Docket No. SA80-8, issued Dec. 13, 1979). We have found nothing in Wallace's petition which persuades us that Wallace is suffering irreparable injury as a result of this rule, and the stay is therefore denied. The Conecuh-Monroe Counties Gas District (Conecuh-Monroe) has replied in opposition to Wallace's application for rehearing. In accordance with 18 C.F.R. § 1.34(d), the Commission will not consider a response to an application for rehearing.

In addition Mobile Gas Service Corp., Scotch Plywood Co. of Alabama and Clarke-Mobile County Gas District filed application for rehearing of Order No. 58 on June 23, 1980; on June 28, 1980 Conecuh-Monroe Counties Gas District, Alabama filed an application for rehearing of that order. We find that these parties have shown no good cause why their application should be considered six months out of time, and therefore we are denying the applications.

first sale in § 270.203 contravenes the language and intent of section 2(21)(B) and other provisions of the NGPA.

On January 9, 1980, the Commission issued an Order Granting Rehearing of Order No. 58 for Purposes of Further Consideration, and subsequently determined that the issues of law and policy raised in these applications should be evaluated in concert with the Commission's final action on rehearing of Order No. 98, promulgating the rule for the pricing of interstate pipeline production under the NGA.[16] Six timely applications for rehearing of Order No. 98 were received.[17] After considering the arguments raised

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[16]Order No. 98, *mimeo* at 7.

[17]Timely applications were filed by Michigan-Wisconsin, Kansas-Nebraska, Northwest Pipeline Company (Northwest), Kentucky-West Virginia, Consolidated and Arizona Electric Power Cooperative, Inc. (AEPCO). No untimely applications were filed. On September 25, the Commission granted rehearing of Order No. 98 for purposes of further consideration. (Docket No. RM80-6, issued September 16, 1980.

AEPCO's application fails to specify any error in Order No. 98, and was admittedly filed only to secure AEPCO's right to participate in any administrative or judicial review of this order with respect to certain issues raised by another party in response to the Notice of Proposed Rulemaking in this docket. *See* AEPCO Motion Requesting Acceptance fo Comments Out of Time and Application for Rehearing, at 2 (Docket No. RM80-6, Sept. 3, 1980). AEPCO states that its "primary concern" in ths proceeding is to oppose comments made by El Paso Natural Gas Company, AEPCO's only gas supplier, in a certain issue raised in the Notice of Proposed Rulemaking in this docket. AEPCO states that it agrees with the Commission's position taken in Order No. 98 and would support that position on judicial review. Consistent with § 1.34(b) of the Commission's Rules of Practice and Procedure, and section 19(a) of the NGA, AEPCO's application is dismissed because AEPCO specifies no error in and does not claim to be aggrieved by Order No. 98.

AEPCO has also moved the Commission to modify its decision in Order No. 98 to refuse to consider out of time AEPCO's late filed comments on the proposed rule in this docket. AEPCO originally submitted comments in Docket No. RM80-6 on June 23, 1980; the

in the applications for rehearing of Order No. 58 and Order No. 98, the Commission is persuaded that its interpretation of section 2(21) of the NGPA is correct, and that the policy of pricing parity for interstate pipelines should be implemented. For reasons stated more fully below, the Commission affirms its rules in § 270.203 and § 154.42 and denies rehearing of Order No. 58 and Order No. 98.

II. Applications for Rehearing of Order No. 58

A. Pricing treatment of mixed volumes sales by pipelines and distributor producers.

The applications for rehearing of Order No. 58 take issue with the interpretation of section 2(21)(B) of the NGPA set forth in § 270.203(a) of the Commission's regulations. MidLouisiana, Kansas-Nebraska,[18] Consolidated and Kentucky West Virginia argue that the language of section 2(21)(B) plainly entitles pipeline producers to NGPA first sale treatment for all volumes of natural gas produced by a pipeline; they believe that the only purpose of section

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comment period had closed on January 14, 1980. The Commission declined to consider these comments noting that they were not submitted prior to Commission consideration of the final rule. Order No. 98 *mimeo* at 6, n.11. AEPCO contends that on June 18, 1980, the date the Commission reached a final decision in this docket, a misunderstanding between AEPCO's counsel and Commission staff occurred, leading AEPCO to believe that the comment priod had been extended until June 23, 1980. AEPCO argues that as a result of this misunderstanding, AEPCO's comments were filed too late for Commission consideration. This alleged misunderstanding, occurring on June 18, does not constitute reasonable grounds for AEPCO's failure to file during the sixty day comment period or prior to the Commission's final action. Therefore AEPCO's motion is denied. 18 C.F.R. § 1.13(d).

[18]The application of Michigan-Wisconsin is identical to the application of Kansas-Nebraska. Any description of the views of Kansas-Nebraska also describes the views of Michigan-Wisconsin.

2(21)(B) is to insure that purchased gas will be excluded from first sale treatment. Kansas-Nebraska suggests that section 2(21)(B) was drafted as an exclusion to the first sale definition in order to distinguish the situation of pipeline and independent producers; such a distinction is necessary, it argues, because a pipeline, unlike an independent producer, sells purchased gas as well as its own production. Applicants conclude that the Commission, in promulgating § 270.203(a), has exceeded the bounds of its statutory authority by adopting of a rule that negates the language and intent of the statutorily prescribed definition of first sale[19] and unlawfully discriminates against pipeline producers.[20]

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[19]Consistent with their view of the attribution rule Kentucky-West Virginia, Mid-Louisiana and Consolidated argue that paragraphs (b) and (c) of § 270.203 (which extend first sale treatment in certain circumstances to sales of pipeline and affiliate production) accomplish the right result for the wrong reason. These applicants believe that the Commission has no discretion to denominate as first sales the sales described in § 270.203(b) and (c), because such sales are in fact first sales by statutory prescription. By using its discretionary authority under section 1(21)(A)(v), to denominate these sales as mixed sales, the Commission, they claim, purports unlawfully to retain the discretion to deny such gas first sale treatment at a later time.

[20]Kansas-Nebraska contends that they have been denied equal protection under the law by the Commission's adoption of § 270.203, because the rule discriminates against pipeline producers *viz-a-viz* other producers. Kentucky-West Virginia argues that they have been denied equal protection *viz-a-viz* pipeline producers with producing affiliates because eligibility for first sale treatment depends solely on corporate form. Also, Kansas-Nebraska argues that the passage of Title I and section 2(21(B) of the NGPA vested in pipeline producers a "property right" that has been deprived them without due process of law.

We find no merit in these arguments. An administrative and legislative classification in economic regulation does not violate the principles of equal protection so long as the classification is rationally related to some legitimate legislative purpose. *United States Dept. of Agriculture*

Some of these commenters also contend that the Commission's interpretation rests on the erroneous assumption that the inclusion of purchased volumes in a sale by a pipeline or distributor deprives those volumes attributable to its own production of first sale treatment. They argue that the Commission can determine what portion of a pipeline's general system supply is attributable to its own production and what portion is composed of purchased gas, and accord first sale treatment to the pipeline produced portion of the sale.

We cannot agree that the plain meaning of section 2(21)(B) guarantees a pipeline the right to collect a first sale price for all volumes of natural gas produced by that pipeline or distributor without regard to the type of transaction or the manner in which the gas is transferred. Section 2(21)(B) speaks in terms of sales, not volumes of natural gas, and excludes a pipeline of distributor sale from first sale treatment "unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline or local distribution company, or any

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v. *Moreno*, 413 U.S. 528, 533 (1973); *Community-Service Broadcast of Mid-America, Inc.* v. *F.C.C.* 593 F.2d 1102, 1122 (D.C. Cir. 1978).

As the foregoing discussion fully demonstrates, distinguishing between wellhead sales and mixed volumes sales is clearly related to the legislative goal of Title I to provide price incentives to encourage production.

Similarly, the due process clause is broadly tolerant of economic price controls. Such economic regulation does not violate the Constitutional guarantees against deprivation of property without due process of law, so long as the regulation is not arbitrary and does not result in confiscation. *E.G., Federal Power COmmission v. Natural Gas Pipeline Co. of America*, 315 U.S. 757, 589-90 (1942). Under the rule of section 2(21)(B) and § 270.203 rates for sales by an interstate pipeline, such as Kansas-Nebraska, will be just and reasonable rates determined according to the Constitutionally sound standards established under the NGA.

affiliate thereof." By the terms of the statute, first sale treatment of a sale made by a pipeline or distributor depends upon the source of the natural gas volumes that comprise the sale. If the source of the volumes that comprise the sale cannot be identified as the pipeline's or distributor's own wells, properties, or reservoirs, the Commission will not accord first sale treatment to the sale. A sale comprised or commingled volumes of purchased gas and pipeline production does not meet this test.

We do not agree with Kansas-Nebraska that the purpose of section 2(21)(B) is simply to distinguish between independent and pipeline producers. By excepting pipeline, distributor and affiliate production from the general definition of first sale contained in Section 2(21)(A), the NGPA distinguishes between pipeline sales from the general system supply and pipeline sales that occur at the wellhead. This distinction is necessary to preserve the existing division between state and federal pipeline regulation and to preserve the NGA cost-of-service ratemaking scheme for sales from an interstate pipeline's general system supply.

As we noted in Order No. 58, the interpretation of section 2(21)(B) advocated by these commenters would result in the uniform application of first sale maximum lawful prices to all mixed volume retail sales made by pipelines and distributors. As a result, rates for retail sales by intrastate pipelines and local distribution companies could not exceed the applicable maximum lawful prices, a result that would preempt the retail ratemaking jurisdiction of state and local agencies. The Commission finds no evidence in 2(21)(B) or in any other provision of the statute that suggests that Congress intended to require the Commission to expand the field of federal ratemaking authority to include all mixed volume retail sales by intrastate pipelines or local distribution companies, the regulation of which has been the historic preserve of the states.

Furthermore, the interpretation espoused by these commenters assumes that the NGPA contemplates a substantial reworking of the Commission's traditional methods for determining an interstate pipeline's cost-of-service. A seller whose sale qualifies as a first sale is entitled to collect a price for that gas no greater than the applicable maximum lawful price plus an allowance for severance taxes and production related costs permitted by the Commission under section 110 of the NGPA. In seeking to determine a rate for a mixed volume sale that would provide for recovery of such costs, the Commission would be forced to discard the complex framework of statutory standards and case law precedent developed under the NGPA for purposes of determining the costs of transporting its sales volumes. Rather than establishing an NGA just and reasonable rate on the basis of the pipeline's cost-of-service, the Commission would determine under its regulations implementing section 110 the costs in excess of the first sale price that a pipeline may recover to compensate it for the transportation and other costs associated with the delivery of its mixed volume sales to its purchasers.

To grant first sale treatment only to an allocable portion of an interstate pipeline's mixed volume sale cures this problem only with respect to the volumes that are allocable to purchased gas. The pipeline would recover the costs associated with the delivery of purchased gas on a traditional cost-of-service basis, permitting the recovery of all costs prudently incurred in accordance with the Commission's regulations. However, for those volumes allocable to pipeline production, the pipeline would be limited to recovery of amounts available under section 110.[21].

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[21] Also, such an allocation would impose an enormous administrative burden upon interstate pipelines and the Commission. The Commission would be required to distinguish scrupulously between

With regard to intrastate pipelines, if the Commission were to accord first sale treatment to some portion of an intrastate pipeline sale, the Commission would be able to determine the section 110 allowance associated with the pipeline production, but would lack jurisdiction to scrutinize the recovery of costs associated with transportation of purchased gas. To the extent that costs allocable to pipeline production were also recovered in the price set by state or local authority, the NGPA maximum lawful price applicable to the pipeline production would be circumvented.

B. **Imputation of a Sale at the Wellhead.**

Recognizing the difficulties of according first sale treatment ot mixed volume sales, Kentucky-West Virginia, Kansas-Nebraska, Mid-Louisiana and Consolidated urge the Commission to impute a sale at the point at which the pipeline takes its production into its general system supply. Consolidated argues that the word "attributable" means "imputable" and, therefore, that the Commission must impute a sale at the wellhead in order to assure a pipeline first sale treatment for all volumes of its own production. Kentucky-West Virginia, Kansas-Nebraska and Consolidated point out that the statement of managers accompanying the NGPA conference report makes clear that the Commission's general rulemaking authority under section 501 of the NGPA includes the power to "establish rules applicable to intracorporate transactions under the

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costs associated with purchased gas and those associated with pipeline production, so that each could be evaluated under the differing regulatory standards of the section 110 regulations and the NGA regulations. The Commission cannot easily assume, without some supporting evidence, that Congress intended to increase so substantially the regulatory burdens of determining the cost-of-service for pipeline producers.

first sale definition."[22] They argue that this language was intended to confer upon the Commission the authority to fully effectuate what they believe to be Congress' intent to accord first sale treatment of some portion of each mixed volume sale.

Mid-Louisiana contends that the delivery into the pipeline of its own production is a transfer for value, and thus meets the definition of "sale" under section 2(20) of the NGPA. Therefore, it argues that the Commission could accord first sale treatment to that intracorporation transaction by exercising its authority under section 2(21)(A)(v) to define that "sale" as a first sale.

The Commission acknowledges its authority under section 501 to impute a sale at the wellhead and thereby to accord first sale treatment to pipeline production. However, we see no mandate implicit in the definition of first sale that requires us to exercise this general authority to any specific end. We believe that the language chosen by the conference managers is clearly designed to delegate to the Commission the discretion to define the term first sale as it may apply to intracorporate transactions.[23]

In its administration of the NGA, the Commission has not treated as a sale the transfer of pipeline produced gas into the transmission system of that pipeline. No contracts govern that transfer; no certificates under the NGA have been issued or were required for that transfer. The proper implementation of the NGPA, which only minimally disturbs the Commission's rules of law that govern pipeline

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[22] *Citing* H. Rep. No. 95-1752, 95th Cong., 2d Sess. 116 (1978). The Joint Statement provides that "(t)he Commission may define terms, prescribe the forms of reports, and prescribe effective dates for rules and regulations. For instance, the Commission may define terms such as 'transfer for value' used in the definition of first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition."

[23] *See* discussion *infra* page 21-23.

ratemaking under the NGA, does not as a practical matter compel us to vary that policy.

To the contrary, we believe that such an interpretation of the term sale would prove difficult to reconcile administratively with certain provisions of the NGPA. For example, the maximum lawful price under section 104 assumes the existence of a just and reasonable rate applicable to the sale of natural gas prior to the enactment of the NGPA. However, because the pipeline's intracorporate transfer was not a sale under the NGA, there was no just and reasonable rate applicable to that transfer. Also, the provisions of section 315, governing the duration of contracts, bona fide offers, and right of first refusal depend upon the existence of a contract for their applicability and effect. These provisions, which provide purchaseres of gas from independent producers with some assurances of continued supply, are inapplicable to a pipeline that "sells" natural gas in a first sale to itself. Absent the contraints of section 315, and the requirement of abandonment authorization that would be inapplicable to gas sold in a first sale, the pipeline's purchasers would have no continuing obligation to offer its purchasers a continued supply of gas from its production properties.

To the extent that this provision and other provisions of the NGPA are conceptually dependent upon the existence of a sale, contract or certificate, the Commission would be required to devise other means by which to insure proper implementation of the statute. We have concluded that the regulation and enforcement of rates for sales of pipeline production should not depend on an event that is recorded solely on the books and records of the pipeline and that occurs without by contract, bargaining, or certification. We decline, therefore, to exercise our discretion in this manner.

C. **Arguments Based on Other Provisions of the NGPA.**

Several applicants argue that other provisions of the NGPA are consistent with their view of section 2(21)(B). Kentucky-West Virginia nad Consolidated maintained that the incremental pricing passthrough provisions demonstrated that Congress intended all pipeline production to be accorded first sale treatment. Section 203(b) provides in, relevant part:

> (b) First Sale Acquisition Costs.-
> (1) GENERAL RULE--For purposes of this section, the first sale acquisition cost of natural gas is-
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> (A) the price paid, per million Btu's, in any first sale of such natural gas, in the case of any natural gas produced in the United States and acquired in such first sale; and
>
> (B) the price paid for such natural gas, per million Btu's, at the point of entry to the United States, in the case of natural gas or liquefied natural gas imported into the United States.
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> * * * *
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> (2) INTERSTATE PIPELINE PRODUCTION.-- For purposes of this section, in the case of any natural gas produced by any interstate pipeline or any affiliate of such natural gas shall be determined in accordance with rules prescribed by the Commission.
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> * * * *

The applicants contend that use of the phrase "first sale acquisition cost" indicates that Congress intend the pipeline's "acquisition" of its own production to be a first sale.

While we understand that these words, isolated from their context, may appear to imply that a true first sale wtihin the meaning of section 2(21)(B) has occurred, we believe that the language of the section as a whole leads to the opposite conclusion. Clause (1)(A) of subsection (b) sets out the general rule permitting passthrough of first sale acquisition costs equal to the "price paid — in any first sale of such natural gas, in the case of any natural gas produced in the United States and acquired in such first sale." In contrast, clause (2) sets out a special rule applicable to interstate pipeline production to provide for passthrough of first sale acquisition costs of such natural gas "determined in accordance with rules prescribed by the Commission." The provision for pipeline production differs notably from the general rule in that it omits any reference to "price paid" and does not indicate that such gas will be "acquired in a first sale." Had Congress intended to mandate that "first sale" include all deliveries of a pipeline's production from the wellhead to its transportation system, it would have been unnecessary to create a separate rule under section 203(b)(2) for pipeline production that expressly contemplates that the acquisition cost of a pipeline's own production will be set by order or rule of the Commission.

Consolidated argues that the Commission's assertion of NGA jurisdiction over certain categories of pipeline production violates section 601 of the NGPA. Consolidated contends that the effect of section 601(a)(1(A) is to terminate the Commission's jurisdiction with respect to any natural gas that was not committed or dedicated to interstate commerce on the effective date of the NGPA. Furthermore, it points out, section 601(a)(1)(B) terminates the Commission's jurisdiction under the NGA over committed or dedicated natural gas that qualifies for an incentive price under section 102(c), 103(c), or 107(c)(1), (2), (3) or (4). On the basis of this language, Consolidated reasons that the Commission's NGA jurisdiction has been

superseded, and that a pipeline should be permitted to collect NGPA prices for all volumes of its own production.[24]

We agree that section 601(a)(1)(A) provides that NGA jurisdiction of gas not previously committed or dedicated to interstate commerce does not survive the NGPA "solely by reason of any first sale of that gas," and concede that section 601 terminates NGA jurisdiction over committed or dedicated gas that qualifies for a maximum lawful price under section 102(c), 103(c), or 107(c)(1), (2), (3) or (4). We note, however, that the scope of each of these provisions in section 601 depends upon the definition of the term first sale, and that neither provision speaks to the question of what types of sales are first sales. Thus, while we acknowledge that section 601 modifies the Commission's NGA jurisdiction with regard to gas sold in first sales, we find nothing in that section that indicates that a mixed volumes sale is a first sale for purposes of section 601 and the NGPA as a whole.

.D. **First Sale Treatment of Sales by Affiliates.**

Wallace Energy Corporation (Wallace) objects to the affiliate rule of § 270.203(c). First, it argues that Congress did not intend to empower the Commission to apply NGPA maximum lawful prices to sales other than wellhead sales. Wallace points out that it is a "paper company" that engages in no production and that has never before been subject to federal regulatory authority. In addition, Wallace contends that the Commission has unconstitutionally extended first sale treatment to sales "without any arguable relationship to interstate commerce." It submits that although producer sales have an impact on interstate commerce, Wallace's activities occur wholly within the state of Alabama.

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[24]See also Consolidated's Application for Rehearing of Order No. 98 (docket No. RM80-6, filed Sept. 3, 1980).

We are not persuaded that the Commission has exceeded its authority under section 2(21)(A)(v). Clearly, as Wallace submits, the underlying purpose of Title I was to provide price incentives for producers and to impose some measure of regularity upon producer sales to the interstate and intrastate gas markets. However, Congress was also aware that middlemen could be used to circumvent price ceilings made applicable only to producers, and that the economic benefits of a systematic pricing scheme would be undercut by an circumvention.[25] In our view, our exercise of the Commission's authority under section 2(21)(A)(v) to treat such sales as first sales implements the express purpose of that authority to prevent circumvention of NGPA maximum lawful prices.

Wallace's contention that the Commission is without constitutional authority to regulate its wholly intrastate transactions ignores the body of constitutional law that defines the federal government's authority under the commerce clause. An act of Congress that reaches any generic category of local activity is a legitimate exercise of the commerce power if the activity has a substantial economic effect on interstate commerce. The fact that Wallace may itself have minimal impact on interstate commerce does not remove it from the scope of regulation where its activity combined with that of other similarly situated middlemen, has a significant impact on interstate commerce.[26] Clearly, Congress was within its constitutional power to authorize the Commission to accord first sale treatment to certain wholly intrastate transactions. The Commission's proper exercise of such authority is equally free of constitutional infirmity.

All other arguments raised in these applications have been addressed in Order No. 58, or in this Order.

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[25]See discussion *supra* note 7.

[26]E.G., *Maryland* v. *Wirtz*, 392 U.S. 183, 193, 196 n.27 (1968).

III. Rehearing of Order No. 98

A. Authority to Establish Rates for Pipeline Production Under the NGA.

Arguments raised on rehearing of Order No. 98, which sets out the Commission's policy regarding pricing of interstae pipeline production under the NGA, concern primarily the question whether the Commission's jurisdiciton to establish such a policy survives the enactment of the NGPA.

Michigan-Wisconsin, Consolidated, Kansas-Nebraska and Kentucky West Virginia object to Order No. 98 as an unlawful assertion of Commission jurisdiction over wellhead prices for pipeline production. They advert to, and incorporate by reference, their applications for rehearing of Order No. 58, in which they argue that the Commission has improperly interpreted section 2(21)(B) of the NGPA to deprive most pipeline production of first sale treatment, thereby excluding such production from eligibility for NGPA maximum lawful prices. They believe that interstate pipelines as a matter of right are entitled to NGPA maximum lawful prices, and therefore, that the Commission's attempt to assert NGA authority to regulate the price of pipeline production is unlawful.

The arguments are not corollaries to the arguments raised on rehearing of Order No. 58, which the Commisison has fully addressed in the foregoing discussion We remain convinced that the language and intent of section 2(21)(B) does not require the Commission to treat mixed volumes sales by pipelines and distributors as first sales.[27] Section 2(21)(B) preserves the Commission's authority under the NGA to regulate such sales made by interstate pipelines, and serves as the jurisdictional

[27]As noted above, the Commission may, in its discretion, treat such sales as first sales, to prevent circumvention of the NGPA maximum lawful prices. *See supra* note 6; § 270.203(b).

predicate for the Commission's implementation of its parity of pricing policy.

B. Exclusion from NGPA Rate Treatment of Natural Gas That Has Ever Been Subject to Cost-of-Service Treatment.

Two applicants object to the Commission's decision to extend NGPA rate treatment only to natural gas produced from leases that have never been subject to cost-of-service treatment, Kentucky, West Virginia and Kansas-Nebraska argue that the Commission erred in its assumption that pipeline whose production has been valued on a cost-of-service basis have recouped their costs and gained substantial benefits from cost-of-service treatment.

Kentucky West Virginia does not agree with the Commission's view that investment costs of old production have necessarily been recouped, and claims that there is no evidence in the record that supports the Commission's conclusion. Kentucky West Virginia also alleges that the cost-of-service exclusion violates the pipeline's right to collect incentive prices for its high cost production and thwarts the Commission's own policy to provide incentives for production of natural gas found in tight formations. Kansas-Nebraska points to Commission precedent in support of its view that a pipeline that has at some time utilized cost-of-service pricing for its own production has not necessarily realized a greater return, as compared to the return it would have realized under area or nationwide rate treatment.[28]

The Commission is not persuaded by these arguments. Kentucky West Virginia's challenge to the Commission's position ignores the essential characteristic of cost-of-

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[28]*Citing* Natural Fuel Gas Supply Corp. (DOcket No. RP76-96 and RP77-57, issued Nov. 14, 1978) *adopted by Commission*, Opinion No. 58 (issued August 6, 1974).

service treatment: a pipeline whose production is valued on a cost-of-service basis will receive a rate that, over time, provides for the recoveryof all prudently incurred costs plus a reasonable return on investment. In the case of production from leases that have received cost-of-service treatment, the pipeline is able to recover the cost of acquiring leases, drilling unsuccessful and successful wells, and producing the reserves, including the opportunity to earn a reasonable return. Any new production from leases that will remain on cost-of-service treatment, including production from tight formations, will also be valued at a rate that will return to the pipeline producer its costs, plus a reasonable return on investment.

In response to Kansas-Nebraska, the Commission emphasizes that the benefits of cost-of-service treatments not that a pipeline is certain to receive greater revenues than it would under area or nationwide rate treatment, although that is often the case. Cost-of-service treatment permits the pipeline producer to invest in exploration and prouction activities while passing on the costs nad risks of that investment to its purchasers. In exchange for assuming the risks of investment, purchasers receive the benefits of additional supplies of natural gas at a nrate no higher than the pipeline's costs plus a reasonable return on investment. To vary this policy now would deprive these purchasers of price benefits they should receive in exchange for assuming the risk of a pipeline's production ventures.

Kentucky West Virginia also argues that although the Commission claims that the cost-of-service exclusion is premised on the need for equitable treatment among independent and pipeline producers, its policy of "limited parity" achieves inequitable results. It contends that the Commission has varied from its prior practices by distinguishing between producing pipelines and pipelines with producing affiliates, providing NGPA rates in all cases for the latter and, in the case of the former, denying parity of

treatment for substantial volumes of natural gas because the gas previously has been subject to cost-of-service treatment. Also, Kentucky West Virginia maintains that the Commission's parity policy is inequitable insofar as it provides NGPA rate treatment for wells drilled after December 31, 1972, on leases acquired before October 8, 1969, but denies parity to wells drilled before January 1 1973 on the same leases.

The Commission finds no merit in these arguments. Sales of gas by producing affiliates of pipelines or distributors (that are not themselves pipelines or distributors) are subject to NGPA maximum lawful prices because such sales are first sales within the meaning of section 2(21)(B) of the NGPA. This is consistent with the treatment accorded such sales under prior practice: under the NGA, transactions between producing affiliates and interstate pipelines were accomplished in the same manner as sales by independent producers, pursuant to contracts and certificates.[29] However, the Commission has exercised its authority under the NGA to value pipeline production for purposes of computing a pipeline's cost-of-service so as to permit parity with independent and pipeline-affiliated producers where appropriate. Thus, the distinction drawn between pipeline affiliates and pipeline producers is based on the allocation of jurisdiction over sales by these entities implied in section 2(21)(B).

In crafting this parity of pricing policy to provide necessary incentives to pipeline producers, the Commission weighed the interests of such pipelines and their purchasers, and determined its was necessary to preserve the price benefits guaranteed to purchasers of production subject to

[29]Section 270.203(a) provides that in according first sale treatment to sales by affiliates of pipelines or distributors, " 'sale' does not include any transaction between an interstate pipeline and an affiliate thereof, if such transaction would not have been treated as a sale for purposes of the Natural Gas Act."

cost-of-service treatment in exchange for assuming the risks of the pipeline's production efforts. The distinction between wells drilled before and after January 1, 1973, on leases acquired before October 8, 1969, represents the distinctions drawn by the Commission when the area and nationwide rates were first applied prospectively to new pipeline production.[30] The continuation of the distinction effectuates the Commission's intent to continue parity of pricing treatment for pipeline production previously subject to area or nationwide rate treatment, *i.e.* production for which pipelines themselves have assumed the risk.

III. Rehearing of Order No.

C. Applicability of the Cost-of-Service Exclusion to Natural Gas That Has Been Subject to Cost-of-Treatment as Result of a Settlement.

In addition to raising a general argument against the cost-of-service exclusion, Kansas-Nebraska raises objections to the provisions of the regulation that continue cost-of-service treatment for pipeline production subject to such treatment by the terms of a settlement. Kansas-Nebraska contends that a finding on the merits of special circumstances under § 2.66(a)(4) is not equivalent to a

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[30]In Opinion No. 568, the FPC initiated the parity pricing policy under which gas produced by a pipeline or its affiliates from leases acquired after October 1, 1969, and taken into the pipeline's own system would be valued by reference to the just and reasonable area rate established for sales by independent producers in the same area. *Pipeline Production* by independent producers in the same area, *Pipeline Production Area Rate Proceeding*, Opinion No. 568-A, supra note 8, 42 F.P.C. at 1091. In Opinion No. 699-H, *mimeo* at 47-50, the FPC reaffirmed its decision that pipeline production from pre-October 8, 1969 leases should continue to be priced on a cost-of-service basis, but concluded that pipeline production from wells drilled on or after January 1, 1973, should be valued at nationwide rates regardless of the date the lease was acquired.

settlement agreement that provides for cost-of-service treatment. It argues that a pipeline granted cost-of-service treatment upon a finding of special circumstances has bargained for on-going cost-of-service treatment in exchange for the opportunity to pass through its risks. This, it reasons, is distinguishable from the situation of a pipeline that negotiates a settlement to resolve a limited number of issues for a specified period of time.[31] Kansas-Nebraska argues, based on Commission precedent, that the Commission may not rely on the terms of a settlement in any future rate proceeding to achieve results that a pipeline had not bargained for in the settlement.[32]

Although we agree that the provisions of a settlement do not bind the parties beyond the term of that settlement, Kansas-Nebraska errs in its conclusion that the terms of a settlement constrain the Commission's authority to determine the scope of applicability of its parity policy. The Commission's decision to deny NGPA rate treatment for gas valued on a cost-of-service basis is not only an attempt to enforce a bargain made by pipeline producers that obtained cost-of-service treatment under th special circumstances provisions. Our decision also rests upon

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[31]Kansas-Nebraska submits that in its particular case the Commission had rejected its attempt to show special circumstances, but subsequently approved a settlement permitting cost-of-service treatment for all of its production that otherwise would have been subject to area or nationwide rate treatment. In Kansas-Nebraska's view, the relevant provisions of that settlement make clear that it was required to file on a cost-of-service basis only in the next subsequent rate proceeding, that the settlement represented a negotiated dollar amount, and that the use of cost-of-service methodology did not imply that any part had approved or consented to any ratemaking principle or theory of allocation.

[32]*Citing Mobile Oil Corp.* v. *FPC*, 570 F.2d 1021 (D.C. Cir. 1978); *Texas Gas Transmission Corp.* v. *FPC*, 441 F.2d 139 (6th Cir. 1971).

assessment that the inherent benefits of cost-of-service treatment, *i.e.* the pipeline's opportunity to pass on the risks of its production programs to its purchasers, requires us to preserve the corresponding benefits that should insure to the pipeline's purchasers. Thus where a pipeline has passed on to its purchasers the risks and costs of acquiring, exploring and developing certain leases, purchases should be entitled to purchase the gas from those leases on a cost-of-service basis.

D. **Termination of Special Circumstances.**

Northwest Pipeline Corporation (Northwest) protests the Commission's decision to deny a pipeline producer subject to NGPA rate treatment the opportunity to seek cost-of-service treatment on the basis of a showing of special circumstances. Northwest notes that in Order No. 568 the Commission encouraged pipeline producers to reinvest amounts in excess of the costs of production collected under area or nationwide rates; Northwest claims that it did reinvest its excess income with the expectation that it could attempt to show special circumstances if the costs associated with that investment provided to be too high. It therefore argues that by eliminating the special circumstances program the Commission has undermined Northwest's investment decisions.

Northwest points out that it has special overriding royalty contracts that provide for royalty payments computed on the basis of a commodity value formula. It reasons that the advent of natural gas deregulation would make these payments very high. Although the Commission has indicated that pipeline producers may be able to address such problems by seeking special relief, Northwest finds that the proposed special relief rule is not appropriate for its purposes.

First Northwest points out that the scope of the proposed special relief rule does not as yet include pipeline producers[33], and does not specifically provide for the recovery of overriding royalty payments as an operating and maintenance expense. Northwest finds unwiedly the requirement that applications for special relief rates to cover on-going operating and maintenance expense must be submitted on a well by well basis, and believes that the proposed ceiling for special relief may prove to be too low to permit Northwest to recover the expense of its royalty payments. Moreover, Northwest argues, the Commission should ot terminate the special circumstances program prior to establishing procedures for special relief. Northwest therefore urges the Commission to restore the special circumstances program so that Northwest would not be required to value its production "at confiscatory levels."

The Commission is not persuaded that the special circumstances program should be reinstated. First, Northwest correctly argues that the purpose of the special circumstances program was to encourage additional pipeline investment in drilling programs that would lead to the development of new reserves. However, the Commission found in Order No. 98 that the NGPA incentive prices were sufficient to induce future drilling efforts of pipeline producers. Furthermore, pipelines that in the past have undertaken new investment were not guaranteed cost-of-service treatment under the special circumstances program; the Commission has consistently found that the fact that a pipeline's costs exceed its revenues is not sufficient to demonstrate special circumstances

[33]The Commission asked for comments on this issue in the Notice of Proposed Rulemaking for Procedures Governing Applications for Special Relief (Docket No. RM79-67, issued May 9, 1980).

warranting cost-of-service treatment.[34] Thus, no pipeline that had not been granted special circumstances undertook new investment with a guarantee that it would subsequently recieve cost-of-service treatment if the costs associated with the investment proved to be too high.

Also, we note that the overriding royalty payments by Northwest are not investment costs. To the extent that special rate treatment would be available to cover such expenses, it would be through application for special releif for a rate covering such payments as operating and maintenance expense. The Commission will address issues related to the scope of the special relief rulemaking in the final rule in that docket.

E. Commission Authority to Prevent Corporate Restructuring to Avoid Cost-of-Service Treatment.

Kentucky West Virginia and Consolidated take issue with the language in Order No. 98 indicating the Commission's intent to use its authority under section 7 of the NGA to prevent a pipeline from spinning off production properties to an affiliate in order to obtain first sale treatment for volumes produced by the affiliate form those properties. Both applicants contend that the Commission lacks authority under the NGA to prevent the transfer of undeveloped leases.[35]

Consolidated submits that section 601(a) terminates the Commission's jurisdiction under the NGA over natural gas that was not committed or dedicated to interstate commerce on November 8, 1978, as well as any natural gas that, although committed or dedicated to interstate commerce on November 8, 1978, qualifies under section 102(c), 103(c), or 107(c)(1)-(4) of the NGPA. Thus, it

---

[34] Order No. 98, *mimeo* at 9, n. 19.

[35] *Citing Federal Power Commission* v. *Panhandle Eastern Pipeline Co.*, 337 U.S. 498 (1949).

argues, the Commission is without authority to scrutinize abandonment under section 7(b) of the NGA with respect to such natural gas.

Kentucky West Virginia points out that section 601(c) of the NGPA provides that the Commission may not deny, or condition the grant of, any certificate under section 7 of the NGA based upon the amount paid in any sale of natural gas, if such amount is deemed to be just and reasonable under subsection (b) of section 601. It reasons, therefore, that the Commission plainly is without authority to condition a transfer of leases to an affiliate so as to require cost-of-service pricing by the affiliate.

The Commission does not agree that it is without authority under the NGA to prevent a pipeline from circumventing the cost-of-service exclusion by corporate restructuring. As noted above, the provision of section 601 of the NGPA constrain the Commission's authority with regard to natural gas sold in first sales. We therefore cannot concede that these provisions circumscribe the Commission's authority with regard to natural gas that remains subject to the Commission pricing jurisdiction under the NGA. Moreover, any jurisdictional challenges to the Commission's use of its authorities under the NGA to prevent circumvention of this rule by corporate restructuring are collateral to issues pertaining to the validity of this rulemaking. The Commission will therefore address such challenges in a more appropriate forum.

III. Clarification of Order No. 98

Since the issuance of Order No. 98, the Commission has received several inquiries regarding the eligiblity of pipeline producers subject to NGPA rate treatment pursant to § 154.42(b)(1) to make interim collections under Part 273 of Subchpater H. Under Part 273, a seller that has filed for a determination of eligibility to collect an incentive price

under certain sections of Title I of the NGPA may collect that price on an interim basis prior to final determination that the well is eligible for such a price.

The Commission did not intend to preclude pipelines subject to NGPA rate treatment from making interim collections under Subchapter H. The Commission intended that the reference to Subchpater H in § 154.42(b)(3) imply this authority. In view of the confusion expressed on this point, we are clarifying § 154.42(b)(1) by expressly referencing the authority under Part 273 for such collections.

Because this amendment effects no substantive change in the rule but is necessary for proper implementation of the rule, the Commission finds that public notice and comment is unnecessary. For the same reasons, the amendment is being made effective October 3, 1980.

The Commission Orders:

1. Applications for rehearing timely filed of Order No. 58 and Order No. 98 are denied;

2. The motion of Wallace Energy Corporation that its application for rehearing of Order No. 58 be deemed timely filed is denied;

3. The late filed application for rehearing of Wallace Energy Corporation is deemed a motion for reconsideration, and is denied;

4. The motion for stay of the effectiveness of Order No. 58 with respect to Wallace Energy Corporation is denied;

5. Late filed applications for rehearing of Order No. 58 by the Conecuh-Monroe Counties Gas District and Mobile Countries Services Corporation, Scotch Plywood Company of Alabama and Clarke-Mobile County Gas District, Alabama are dismissed;

6. Response of Conecuh-Monroe Counties Gas District to the Application of Rehearing of Order No. 58 of Wallace Energy Corporation is dismissed;

7. Application for Rehearing of Order No. 98 of Arizona Electric Power Cooperative, Inc. and the City of Willcox, Arizona is dismissed, for failure to specify error in that order;

8. The motion of Arizona Electric Power Cooperative, Inc. and the City of Willcox, Arizona to modify the Commission's decision in Order No. 98 to consider untimely filed comments is denied.

9. Order No. 98 is clarified by amending § 154.41(b)(1)(i) of the Commission's regulations as set forth above, effective October 3, 1980.

(Natural Gas Policy Act of 1978, 15 U.S.C. §3301 *et seq.;* Natural Gas Act, as amended, 15 U.S.C. §717, *et seq.;* Department of Energy Organization Act, 42 U.S.C. §7107 *et seq.;* Exec. Order No. 12009, 42 Fed. Reg. 46267)

In consideration of the foregoing, Part 154 of the Subchapter E, Chapter I, Title 18, Code of Federal Regulation is amended as set forth below, effective october 3, 1980.

(S E A L)

Lois D. Cashell,
Acting Secretary.

Section 154.42(b)(1)(i) is amended by deleting the word "or" following "Part 271" and inserting in lieu thereof a comma, and by inserting the words "or under part 273" following the words "part 272."

C-1

United States Court of Appeals

FOR THE FIFTH CIRCUIT*

Unit A

NO. 80-3804

MID-LOUISIANA GAS COMPANY, *ET AL.*,
Petitioners,

versus

FEDERAL ENERGY REGULATORY COMMISSION
Respondent.

.....

Petitions for Review of Orders of the Federal Energy Regulatory Commission

.....

Before CHARLES CLARK, GARZA and SAM D. JOHNSON, Circuit Judge

JUDGMENT

This cause came on to be heard on petitions of Mid-Louisiana Gas Company, et al for review of orders of the Federal Energy Regulatory Commission, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that Order No. 58 of the Federal Energy Regulatory Commission is hereby vacated;

IT IS FURTHER ORDERED that Intervening-Respondents, Public Service Commission of th State of New York, Arizona Electric Power Cooperative, Inc. and State of Michigan, et al. pay to petitioners, Kentucky-West Virginia Gas Company, et al, Mid-Louisiana Gas Company, et al, Ciba-Geigy Corp., et al and Northwest Pipeline Corporation, the costs on appeal.

December 23, 1981

ISSUED AS MANDATE: March 2, 1982

*Former Fifth Circuit case, Section 9(1) of Public Law 96-452, October 14, 1980.

C-2

United States Court of Appeals

MEMORANDUM TO COUNSEL OR PARTIES LISTED BELOW

No. 80-3804 - Mid-Louisiana Gas Company v. FERC

The following action has been taken in the above cases:

☒ An EXTENSION OF TIME has been granted to and including January 20, 1982 *ONLY***

- ☐ for filing appellant's/petitioner's brief.
- ☐ for filing appellee's/respondent's brief.
- ☐ for filing reply brief.
- ☐ for filing petition for rehearing. (Intervenors)
- ☐

☐ Motion to consolidate granted.
☐ Motion to supplement or correct the record granted.
☐ Motion for leave to file supplemental brief granted.
☐ Motion for leave to file brief *amicus curiae* is granted.
☐ Joint motion as to time for filing briefs granted.
☐ Order enclosed has been entered.

GILBERT F. GANUCHEAU, Clerk

By: _____
Deputy Clerk

**Petition for Rehearing must by physically in Clerk's office by this date.

MOT-2

cc: All Counsel

WILNER & SCHEINER
JAN 13 Rec'd
WASHINGTON, D.C.

FIFTH CIRCUIT
OFFICE OF THE CLERK
800 Camp Street
New Orleans, LA 70130
January 11, 1982
Gilbert F. Ganucheau
Clerk

COMM.	FTS
(504) 589	682

CASE INQUIRIES	
LA	6194
No. & West, TX	4157
So. & East, TX	8131
MS & Agency	3892
Other	6514

C-3

IN THE

United States Court of Appeals

FOR THE FIFTH CIRCUIT

UNIT A

NO. 80-3804

MID LOUISIANA GAS COMPANY, ET AL,
Petitioners,

versus

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

No. 80-4010

CONSOLIDATED GAS SUPPLY CORPORATION, *ET AL.,*
Petitioners,

versus

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent.

.....

Petitions for Review of Orders of the Federal Energy Regulatory Commission

.....

ON PETITION FOR REHEARING AND SUGGESTIONS FOR REHEARING EN BANC

(Opinion December 23, 5 Cir., 1981, F.2d).

(February 5, 1982)

Before CHARLES CLARK, GARZA AND SAM D. JOHNSON, Circuit Judges

PER CURIAM:

(X) The Petition for Rehearing is DENIED and no member of this panel nor Judge of this Administrative Unit in regular active service having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure; Local Fifth Circuit Rule 16; Fifth Circuit Judicial Council Resolution of January 14, 1982), the suggestions for Rehearing En Banc are DENIED.

( ) The Petition for Rehearing is DENIED and the jduges in regular active service of this Administrative Unit having been polled at the request of one of said judges and a majority of said judges not having voted in favor of it (Rule 35, Federal Rules of Appellate Procedure; Local Fifth Circuit Rule 16; Fifth Circuit Judicial Council Resolution of January 14, 1982), the suggestions for Rehearing En Banc are also DENIED.

( ) A member of this Administrative Unit in active service having requested a poll on the reconsideration in this cause en banc, and a majority of the judges in active service of said unit not having voted in favor of it, rehearing en banc is DENIED.

CLERK'S NOTE:
SEE RULE 41 FRAP AND LOCAL
RULE 17 FOR STAY OF THE MANDATE

U.S. COURT OF APPEALS
FILED
FEB. 5, 1982

GILBERT E. GANUCHEAU
CLERKS

APPENDIX D
STATUTES

Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301, *et seq.*
Sections 2(20) and 2(21), 15 U.S.C. §§ 3301(20) and (21).

SEC. 2 DEFINITIONS.

* * *

(20) SALE. — The term "sale" means any sale, exchange or other transfer for value.

(21) FIRST SALE.—

(A) GENERAL RULE.—The term "first sale" means any sale of any volume of natural gas—

(i) to any interstate pipeline or intrastate pipeline;
(ii) to any local distribution company;
(iii) to any person for use by such person;
(iv) which precedes any sale described in clauses (i), (ii), or
(iv) which precedes any sale described in clauses (i), (ii), or (iii); and
(v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this Act.

(B) CERTAIN SALES NOT INCLUDED.-CLAUSES (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

Section 101, 15 U.S.C. § 3311.

Section 101. INFLATION ADJUSTMENT; OTHER GENERAL PRICE CEILING RULES

. . .

(b)(9) EFFECT ON CONTRACT PRICE.—IN THE CASE OF _____

(A) any price which is established under any contract for the first sale of natural gas and which does not exceed the applicable maximum alwful price under this subchapter, or

(B) any price which is established under any contract for the first sale of natural gas which is exempted under part B of this subchapter from the application of a maximum lawful price under this subchapter,

such maximum lawful price, or such exemption from such a maximum lawful price, shall not supersede or nullify the effectiveness of the price established under such contract.

Section 203, 15 U.S.C. § 3343

Section 203. ACQUISITION COSTS SUBJECT TO PASSTHROUGH

. . .

(b) FIRST SALE ACQUISITION COSTS.—

(1) General rule.—For purposes of this section the first sale acquisition cost of natural gas is—

(A) the price paid, per million Btu's, in any first sale of such natural gas, in the case of any natural gas produced in the United States and acquired in such first sale; and

(B) the price paid for such natural gas, per million Btu's, at the point of entry to the United

States, in the case of natural gas or liquefied natural gas imported into the United States.

Any amount of State severance taxers paid at any first sale shall not be included under subparagraph (A) or (B).

(2) Interstate pipeline production.—For purpose of this section, in the case of any natural gas produced by any interstate pipeline or any affiliate of such pipeline, the first sale acquisition cost of such natural gas shall be determined in accordance with rules prescribed by the Commission.

Section 501, 15 U.S.C. § 3411

Section 501. GENERAL RULEMAKING AUTHORITY

(a) In general.—Except where expressly provided otherwise, the Commission shall administer this chapter. The Commission, or any other Federal officer of agency in which any function under this chapter is vested or delegated, is authorized to perform any and all acts (including any appropriate enforcement activity), and to prescribe, issue, amend, and rescind such rules and orders as it may find necessary or appropriate to carry out its functions under this chapter.

(b) Authority to define terms.—Except where otherwise expressly provided, the Commission is authorized to define, by rule, accounting, technical, and trade terms used in this chapter. Any such definition shall be consistent with the definitions set forth in this chapter.

Section 601, 15 U.S.C. § 3431

Sec. 601. COORDINATION WITH THE NATURAL GAS ACT

. . .

(b)(1)(E) Affiliated Entities Limitation.—

For purposes of paragraph (1), in the case of any first sale between any interstate pipeline and any affiliate of such pipeline, any amount paid in any first sale shall be deemed to be just and reasonable if, in addition to satisfying the requirements of such paragraph, such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.

Section 602, 15 U.S.C. § 3432.

SEC. 602. EFFECT ON STATE LAW.

(a) AUTHORITY TO PRESCRIBE LOWER MAXIMUM LAWFUL PRICES.—Nothing in this Act shall effect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under title I of this Act.

(b) COMMON CARRIERS.— No person shall be subject to regulation as a common carrier under any provision of Federal or State law by reason of any transportation—

(1) pursuant to any order under section 302(c) or section 303(b), (c), (d), or (i) of this Act; or

(2) authorized by the Commission under section 311(a) of this Act.

Opposition

1

FILED
AUG 5 1982
ALEXANDER L. STEVAS,
CLERK

Nos. 81-1889, 81-1958, 81-2042, and 82-19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*,

Petitioners,

v.

MID LOUISIANA GAS COMPANY, *et al.*,

Respondents.

On Petitions For A Writ Of Certiorari
To The United States Court Of Appeals
For The Fifth Circuit

BRIEF OF RESPONDENT MID LOUISIANA GAS COMPANY IN OPPOSITION

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August 4, 1982

DI CESARE - Printing — 331-4141 — Washington, D.C. 20004

QUESTION PRESENTED

Whether the court below properly determined that Congress intended the incentive pricing structure of the Natural Gas Policy Act of 1978 to be applied equally to all natural gas production, including production by interstate pipelines, rather than to only the production of independent and affiliated producers.

PARTIES BELOW

American Gas Association
Arizona Electric Power Cooperative and City of Wilcox
Ciba-Geigy Corporation
Colorado Interstate Gas Company
Columbia Gas Transmission Corp.
Consolidated Gas Supply Corp.
Ecee, Inc.
El Paso Natural Gas Company
The Federal Energy Regulatory Commission
Kansas-Nebraska Natural Gas Company
Kansas State Corporation Commission
Kentucky-West Virginia Natural Gas Company
Michigan-Wisconsin Pipe Line Company
Mid Louisiana Gas Company*
Natural Gas Pipeline Co. of America
Northern Natural Gas Company
Northwest Pipeline Corp.
The Public Service Commission of the State of New York
The Public Service Commission of Wisconsin
The State of Michigan and the Public
Service Commission of Michigan
Southern Natural Gas Company
United Gas Pipe Line Corp.

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*Mid Louisiana Gas Company, a respondent in this proceeding, is a wholly-owned subsidiary of Celeron Corporation (formerly Central Louisiana Energy Corporation). In addition, Mid Louisiana is an affiliate of Celeron Oil and Gas Company (formerly South Louisiana Production Company, Inc.), Louisiana Intrastate Gas Corporation, Trans Louisiana Gas Company, Inc., and LIG Chemical Company.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
PARTIES BELOW	ii
TABLE OF CONTENTS	iii
TABLE OF AUTHORITIES	iv
OPINIONS AND ORDERS BELOW	2
JURISDICTION	2
STATUTES INVOLVED	2
STATEMENT OF THE CASE	3
I. Regulatory Background	4
II. The Natural Gas Policy Act of 1978	7
III. Proceedings Before the Commission	8
IV. The Decision Below	10
SUMMARY OF ARGUMENT	12
ARGUMENT	12
A. The Court Below Fully Considered And Properly Rejected Each Of The Arguments Made By Petitioners And Amici	12
B. The Allegations Of Economic Impact Are Inaccurate And Provide No Basis For Review Of The Decision Below	25
C. The Decision Below Does Not Conflict With The Order Of The Supreme Court Of Appeals Of West Virginia In The Pennzoil Case	28
CONCLUSION	30

TABLE OF AUTHORITIES

COURT CASES **Page**

American Tobacco Company v. Patterson, No. 80-1199 (April 5, 1982) 24

American Public Gas Association v. F.P.C., 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978) 5

City of Chicago v. F.P.C., 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972) 6

Colautti v. Franklin, 439 U.S. 379 (1979) 14

Federal Election Commission v. Democratic Senatorial Campaign Committee, No. 80-939 (November 10, 1981) 25

International Brotherhood of Teamsters v. Daniel, 439 U.S. 551 (1979) 13

Mobil Oil Corporation v. F.P.C., 417 U.S. 283 (1974) 18

Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 5

Phillips Petroleum Company v. Wisconsin, 347 U.S. 672 (1954) 4

Shell Oil Company v. F.P.C., 520 F.2d 1061 (5th Cir. 1976), *cert. denied*, 426 U.S. 941 (1976) 5, 22

Volkswagenwerk v. Federal Maritime Commission, 390, U.S. 261 (1968) 25

Wisconsin v. F.P.C., 373 U.S. 294 (1963) 5

STATUTES **Page**

Natural Gas Act, 15 U.S.C. 717, *et seq.* 4, 7, 19

Natural Gas Policy Act of 1978, 15 U.S.C. 3301, *et seq.* ..... *passim*

§ 2(20), 15 U.S.C. 3301(20) 2, 18
§ 2(21), 15 U.S.C. 3301(21) 2, 4
§ 2(21)(A), 15 U.S.C. 3301 (21)(A) 7, 13
§ 2(21)(A)(v), 15 U.S.C. 3301(21)(A)(v) 16
§ 2(21)(B), 15 U.S.C. 3301(21)(B) 7, 8, 11, 13
§ 101(b)(9), 15 U.S.C. 3311(b)(9) 21
§ 201, 15 U.S.C. 3341 8
§ 203(b)(1), 15 U.S.C. 3343(b)(1) 8, 14
§ 203(b)(2), 15 U.S.C. 3343(b)(2) 8, 14
§ 501, 15 U.S.C. 3411 ..... 8, 16, 19
§ 501(b), 15 U.S.C. 3411(b) 8
§ 602, 15 U.S.C. 3432 29

ADMINISTRATIVE ORDERS, OPINIONS, AND REGULATIONS

Order No. 58, Final Rule Governing the Maximum Lawful Price for Pipeline, Distributor, or Affiliate Production, Docket No. RM80-7 (November 14, 1979) 3, 18, 10

Order No. 98, Final Rule Governing Price of Pipeline Production Under the Natural Gas Act, Docket No. RM80-6 (August 4, 1980) 5, 10, 11, 20, 22

Order No. 102, Order Denying Rehearing of Order No. 58 and Order No. 98 and Clarifying Order No. 98, Docket Nos. RM 80-6 and RM 80-7 (October 3, 1980) 10

Opinion No. 568, *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738 (1969) 6

Page

Opinion No. 699-H, *Just and Reasonable National Rates for Sales of Natural Gas*, 52 F.P.C. 1604 (1974) 5, 6

Opinion No. 770-A, *National Rates for Jurisdictional Sales of Natural Gas*, 56 F.P.C. 2698 (1976) 5

Permian Basin Area Rate Proceeding, 34 F.P.C. 159 (1965) 5, 22

MISCELLANEOUS

18 C.F.R. 154.38(d)(4) (1980) 21

43 *Federal Register* 56448 (1978) 8

124 *Cong. Rec.* H13114 (daily ed. October 14, 1978) 15, 25

House Interstate and Foreign Commerce Committee, Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978, H.R. Pub. No. 95-62, 95th Cong., 2d Sess. (1978) 15, 17

H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. (1978) 15, 19

S. Rep. No. 95-436, 95th Cong., 1st Sess. (1977) 16

S. Rep. No. 96-43, 96th Cong., 1st Sess. (1979) 15

Statistics of Interstate Natural Gas Pipeline Companies-1979, U.S. Department of Energy (October, 1980) 27

Nos. 81-1889, 81-1958, 81-2042, and 82-19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*,

Petitioners,

v.

MID LOUISIANA GAS COMPANY, *et al.*,

Respondents.

On Petitions For A Writ Of Certiorari
To The United States Court Of Appeals
For The Fifth Circuit

BRIEF OF RESPONDENT MID LOUISIANA GAS COMPANY IN OPPOSITION

Mid Louisiana Gas Company ("Mid Louisiana"), a petitioner below and a respondent in these proceedings, hereby opposes the petitions for a writ of certiorari filed by the Public Service Commission of the State of New York ("New York") in No. 81-1889, Arizona Electric Power Cooperative, Inc. ("AEPCO") in No. 81-1958, the State of Michigan ("Michigan") in No. 81-2042, and the Federal Energy Regulatory Commission ("Commission") in No. 82-19. Each of these petitions seeks review of the decision and judgment rendered by the United States Court of Appeals for the Fifth Circuit on December 23, 1981, in *Mid Louisiana Gas Company, et al.* v. *Federal Energy Regulatory Commission,* Case No. 80-3804, and *Consolidated Gas Supply Corporation* v. *Federal Energy Regulatory Commission,* Case No. 80-4010.

OPINIONS AND ORDERS BELOW

The opinion of the court of appeals is reported at 664 F.2d 530 and is reproduced in Appendix A to New York's petition.[1] The orders vacated by the court of appeals are not officially reported, but are set forth in Appendix B.

JURISDICTION

The judgment of the court of appeals was entered on December 23, 1981 (App. C-1). Petitions for rehearing filed by New York, Michigan, and AEPCO were denied on February 5, 1982 (App. C-3 to C-4). On April 23, 1982, Justice White granted the Solicitor General an extension of time to and including June 5, 1982, within which to file a petition for a writ of certiorari on behalf of the Commission. On May 27, 1982, Justice White granted the Solicitor General a further extension to and including July 5, 1982, within which to file the petition. This Court's jurisdiction is invoked under 28 U.S.C. 1254(1) and 15 U.S.C. 3416(a)(4).

STATUTES INVOLVED

This case involves the Natural Gas Policy Act of 1978, 15 U.S.C. 3301, *et seq.*, pertinent portions of which are set forth in Appendix D. Particularly relevant are the definitions of "sale" and "first sale" which are set forth, respectively, in Sections 2(20) and 2(21) of the NGPA, 15 U.S.C. 3301(20) and (21):

> "Sale. -- The term 'sale' means any sale, exchange, or other transfer for value."

***

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[1]All appendix citations refer to the appendix filed in No. 81-1889 by New York, the initial petitioner in these proceedings.

"First sale.--

(A) General rule.-- The term 'first sale' means any sale of any volume of natural gas --

(i) to any interstate pipeline or intrastate pipeline;

(ii) to any local distribution company;

(iii) to any person for use by such person;

(iv) which precedes any sale described in clauses (i), (ii), or (iii); and

(v) which precedes or follows any sale described in clauses (i), (ii), and (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this chapter.

(B) Certain sales not included.--Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof."

STATEMENT OF THE CASE

This case involves the applicability of the incentive ceiling prices established by the Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. 3301, *et seq.*, to natural gas which is produced by natural gas pipeline companies and, prior to sale, is commingled with gas purchased from others. In Order No. 58 (App. B-1), the Commission determined that pipeline companies cannot recover the NGPA prices for such production,

because neither the intracorporate transfer of the gas from the pipeline's production facilities to its transmission system, nor the ultimate sale of the gas to downstream customers, constitutes a "first sale" within the meaning of Section 2(21) of the Act, 15 U.S.C. 3301(21). On petitions for review filed by Mid Louisiana and others, Order No. 58 was reversed and vacated by the United States Court of Appeals for the Fifth Circuit. The court specifically held that Congress intended the NGPA pricing structure to apply to *all* natural gas production, without regard to whether the producer is an independent producer, a pipeline, a distributor, or an affiliate of a pipeline or distributor (App. A).

I. Regulatory Background

Prior to the NGPA, the pricing of all natural gas produced and sold for resale in interstate commerce was regulated by the Commission under the Natural Gas Act, 15 U.S.C. 717, *et seq.*[2] Initially, all production (whether produced by an independent producer, pipeline, or pipeline affiliate) was priced on an individual cost-of-service basis.[3] By 1960, however, it became apparent that regulating several thousand independent producers on an individual basis was administratively infeasible. As a result, the Commission abandoned the individual cost-of-service approach for independent producers, and began regulating such sales through the establishment of uniform rates for all

[2]As used herein, "Commission" refers, as appropriate, to either the Federal Energy Regulatory Commission or its predecessor, the Federal Power Commission.

[3]Production by interstate pipelines and pipeline affiliates was regulated by the Commission from the inception of the Natural Gas Act in 1938. Sales by independent producers, however, were not regulated until after this Court's decision in *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672 (1954).

producers within certain areas. See *Wisconsin* v. *F.P.C.*, 373 U.S. 294 (1963); *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968). Subsequently, the Commission's regulation of independent producers shifted from area rates to nationwide rates.[4]

The methodology used by the Commission in the establishment of area and nationwide rates, like that historically used in individual cost-of-service ratemaking, was designed to provide independent producers with recovery of all reasonable costs of exploration, development, and production, including the costs of lease acquisitions and "dry holes".[5] Under the area and nationwide approach, however, the rates established by the Commission were based upon average costs, rather than individual company costs. This created a risk that an independent producer would earn a comparatively lower return if its individual costs were higher than average costs. Conversely, the independent producer enjoyed the opportunity to earn a comparatively higher return if its costs were lower than the average.

Although the Commission shifted to area rates for independent producers, it continued to regulate all sales of production by pipelines and affiliates on a cost-

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[4]See Opinion No. 699-H, *Just and Reasonable National Rates for Sales of Natural Gas*, 52 F.P.C. 1604 (1974), affirmed *sub nom. Shell Oil Company* v. *F.P.C.*, 520 F.2d 1061 (5th Cir. 1976), *cert. denied*, 426 U.S. 941 (1976); see, also, Opinion No. 770-A, *National Rates for Jurisdictional Sales of Natural Gas*, 56 F.P.C. 2698 (1976), affirmed *sub. nom. American Public Gas Association* v. *F.P.C.*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978).

[5]See, e.g., *Permian Basin Area Rate Proceeding*, 34 F.P.C. 159, 192 (1965), affirmed *sub nom. Permian Basin Area Rate Cases*, 390 U.S. 747 (1968). See, also, Commission's discussion in Order No. 98 (App. B-24 to B-25).

of-service basis until October 7, 1969. On that date, however, the Commission recognized in Opinion No. 568 that treating pipelines and affiliates in parity with independent producers would encourage additional exploration and development for new supplies.[6] Accordingly, the Commission ruled that pipelines would be allowed to receive the applicable area rates for all gas produced from leases acquired after the date of the order.

In Opinion No. 699-H, which established the first nationwide rates for independent producers, the Commission expanded its policy by ruling that pipelines and affiliates, like independent producers, could collect the applicable area or nationwide rates for any gas produced from a well drilled on or after January 1, 1973, without regard to lease acquisition date.[7] In taking this additional step toward parity, the Commission reasoned that the "natural gas shortage requires the best efforts of all persons whether producer, pipeline, or pipeline affiliate to explore for and develop new supplies of gas to satisfy existing unfilled demands."[8]

Notwithstanding these initiatives, complete price parity between pipeline production and production by independent producers was not achieved prior to the NGPA. All pipeline production from pre-1973 wells on pre-October 8, 1969 leases continued to be priced by the Commission on an individual cost-of-service basis.

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[6]Opinion No. 568, *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738 (1969), affirmed *sub nom. City of Chicago v. F.P.C.*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972).

[7]Opinion No. 699-H, *supra*, 52 F.P.C. at 1634-1636.

[8]Opinion No. 699-H, *supra*, 52 F.P.C. at 1636.

II. The Natural Gas Policy Act of 1978

With the severe gas shortages which plagued the nation during the mid-1970's, it became apparent that the Commission's regulation of natural gas prices under the Natural Gas Act was flawed in two major respects. First, since the Natural Gas Act provided for federal regulation of only the interstate market, gas could be sold in the intrastate market at substantially higher prices than those permitted by the Commission. As a result, producers had little or no incentive to make significant long-term dedications of gas to the regulated interstate market. Second, the Commission's historic and entrenched cost-based approach to the pricing of gas sold in interstate commerce had failed to provide sufficient economic incentives for the development of new gas supplies.

In response to these problems, and to enhance the nation's future energy security, Congress passed the NGPA in November of 1978. Among other things, the Act established a comprehensive and uniform pricing structure for all "first sales" of natural gas. A "first sale" was generally defined by Section 2(21)(A) to mean "any sale of any volume of natural gas" to an interstate or intrastate pipeline, a local distribution company, or any end user. 15 U.S.C. 3301(21)(A). This provision was qualified, however, by Subsection 2(21)(B), which stated that a "first sale" —

> "...shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or affiliate thereof, *unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or affiliate thereof.*" 15 U.S.C. 3301(21)(B) (emphasis added).

The NGPA also contained incremental pricing provisions which essentially required the Commission to promulgate rules for the pass-through to certain industrial customers of a portion of all "first sale acquisition costs." 15 U.S.C 3341, *et seq.* For this purpose, the "first sale acquisition cost" for any gas *acquired* by a pipeline in a first sale was generally defined by Section 203(b)(1) of the Act to be the "price paid." 15 U.S.C. 3343(b)(1). With respect to gas *produced* by a pipeline, however, the Act provided that "the first sale acquisition cost" of such natural gas shall be determined in accordance with rules prescribed by the Commission." 15 U.S.C. 3343(b)(2).

Section 501 of the NGPA vested the Commission with general rulemaking authority to administer the Act. 15 U.S.C. 3411. Included within this delegation was the authority to define various accounting, technical, and trade terms used in the Act, but only to the extent consistent with the definitions set forth by Congress. 15 U.S.C. 3411(b).

III. Proceedings Before the Commission

On November 14, 1979, pursuant to its rulemaking authority, the Commission issued Order No. 58 (App. B-1 to B-13), which promulgated final regulations governing the applicability of the NGPA to production by pipelines, distributors, and affiliates. Adhering to an interpretation first announced in its interim regulations,[9] the Commission ruled that a sale of natural gas by an interstate pipeline, intrastate pipeline, or local distribution company is not "attributable" to volumes produced by such company, within the meaning of Section 2(21)(B), 15 U.S.C. 3301(21)(B), and, therefore, is not entitled to the applicable "first sale" price under the NGPA, unless such sale is "*comprised exclusively* of production volumes ... from identifiable

[9] 43 *Fed. Reg.* 56448 (1978).

wells, properties, or reservoirs which are owned by such pipeline or distributor." (App. B-12, emphasis added). Under this definition, pipeline production would qualify as a "first sale" in only two situations: (1) where there is an off-system sale at the pipeline's wellhead, and (2) where a downstream sale involves delivery of gas from an identifiable source which has been dedicated by contract to a particular customer (App. B-2 to B-4).

In rendering this interpretation of the Act, the Commission recognized that the vast majority of pipeline production is neither sold at the wellhead, nor contractually dedicated to particular customers, but, instead, is simply combined with gas purchased from others to form a general system supply which is then used to serve all customers. As a result, the Commission conceded that "most sales by interstate pipelines will not qualify as first sales ...". (App. B-3). Notwithstanding this concession, however, the Commission remained adamant in its position, stating that it would not accord "first sale" status to pipeline production sold in mixed volumes, even if it were permitted by the NGPA, because such action would create administrative difficulties and encroach upon state jurisdiction over retail sales by all pipelines and local distribution companies (App. B-4 to B-5).

To avoid the problems envisioned by the Commission in treating the downstream sale of a pipeline's production as the "first sale" under the NGPA, several parties proposed that a "first sale" be imputed at the pipeline's wellhead, where there is an intracorporate transfer of the gas from production facilities into the transmission system. In response to this suggestion, the Commission acknowledged that it had authority to resolve the problem in this manner (App. B-65), but declined to do so, reasoning that intracorporate transfers are not governed by contracts and certificates,

and had not been historically treated as sales under the Natural Gas Act (App. B-65 to B-66).

Despite its determination in Order No. 58 that pipelines are not entitled to the NGPA rates as a matter of *law*, the Commission, on August 4, 1980, issued Order No. 98 (App. B-14 to B-49), ruling, as an exercise of its perceived *discretion*, that interstate pipelines could collect the NGPA rates for all pipeline production which formerly qualified for the area or nationwide rates (i.e., production from post-1972 wells or post-October 7, 1969 leases), provided the applicable NGPA rates do not exceed "the amount paid in comparable sales" between unaffiliated entities (App. B-47). The Commission emphasized, however, that all pipeline production previously subject to cost-of-service treatment would continue to be regulated on that basis under the Natural Gas Act (App. B-14 to B-15, B-27).

On October 3, 1980, the Commission issued Order No. 102, which denied rehearing of Order Nos. 58 and 98 (App. B-50 to B-82). Shortly thereafter, petitions for review were filed by Mid Louisiana and other pipelines in the United States Court of Appeals for the Fifth Circuit.

IV. The Decision Below

On December 23, 1981, the court of appeals issued its decision (App. A) vacating Order Nos. 58, 98, and 102. Summarizing its decision, the court stated (App. A-15):

> "Relying on the language, purposes, and history of the NGPA, we hold that Congress clearly intended for any production attributable to an 'interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof' to be accorded first sale status under the NGPA and that Congress contemplated that the

> intracorporate transfer of pipeline production to the pipeline would be treated as the first sale."

In reaching this conclusion, the court of appeals made essentially three findings. First, after a thorough analysis of the NGPA, the court determined that the Commission's exclusionary interpretation of "first sale" was inconsonant with the language of the Act, particularly Section 2(21)(B), 15 U.S.C. 3301(21(B), which deals with "first sales" of volumes attributable to pipeline production (App. A-8 to A-9). Second, the court found that excluding production by pipelines and distributors from the incentive pricing structure of the NGPA would be inconsistent with the two overriding purposes of the Act, namely, (1) elimination of the dual interstate and intrastate market, and (2) encouragement of new exploration and development (App. A-9). Finally, the court found that the Commission's narrow interpretation of "first sale" was contrary to the legislative history of the Act (App. A-10).

The court emphasized that according "first sale" status to pipeline production would not encroach upon state jurisdiction over retail sales by intrastate pipelines and local distribution companies. This jurisdiction "would remain intact," the court reasoned, the only change being that the retail price established by the states would reflect "the NGPA cost of gas" (App. A-13). The court also expressed confidence that the Commission had adequate rulemaking authority, as demonstrated by Order No. 98, to overcome any administrative difficulties arising from the fact that intracorporate transfers are not governed by contracts (App. A-14).

In vacating the Commission's orders, the court recognized that the Commission's interpretation of the NGPA was entitled to a certain amount of deference. In the final analysis, however, the court was unable to

accept an interpretation "which could challenge the clear meaning" of the statute "as revealed by its language, purpose and history." (App. A-7).

SUMMARY OF ARGUMENT

While the decision below is significant, to the extent it precludes further discrimination against pipeline producers in the application of the NGPA incentive prices, petitioners and amici have failed to demonstrate special and important reasons which would justify further review by this Court. As demonstrated by a brief analysis of the decision below, the court of appeals carefully reviewed and properly rejected each of the contentions now raised by petitioners and amici. In reaching its decision, the lower court did not depart from the accepted and usual course of judicial proceedings. To the contrary, its analysis of the language, legislative history, and purposes of the NGPA was carefully guided by well-established principles of statutory construction. Nor did the court render a decision which is in conflict with any decision of this Court, another federal court of appeals, or a state court of last resort. Under these circumstances, and in view of the court of appeals' thorough and well-reasoned disposition of the issues, the petitions should be denied.

ARGUMENT

A. The Court Below Fully Considered And Properly Rejected Each Of The Arguments Made By Petitioners And Amici.

1. Petitioners and amici argue broadly that there is no evidence that Congress intended for pipeline producers to participate in the price incentives established by the NGPA.[10] As the court below ruled however, the language, legislative history, and pur-

[10]Commission Pet. 20; New York Pet. 11-17; Michigan Pet. 10-19; AEPCO Pet. 15-19.

poses of the NGPA demonstrate conclusively that Congress intended the incentive prices to apply to all natural gas production, without regard to the corporate status of the producer.

The language of the NGPA, which is the starting point for ascertaining Congressional intent,[11] is uncommonly clear and straight-forward. Section 2(21) states that the term "first sale" shall mean "*any* sale of *any* volume of natural gas" to any pipeline, distribution company, or end user. 15 U.S.C. 3301(21)(A) (emphasis added). The only exception is found in Subsection (B) — the so-called "unless clause" — which provides, among other things, that a "first sale" shall not include a sale by an interstate pipeline, "unless such sale is attributable to volumes of natural gas produced by such interstate pipeline...". 15 U.S.C. 3301(21)(B). The obvious purpose of this exception was to insure that the "first sale" ceiling prices did not apply to *subsequent resales* of gas which is purchased by the pipeline in a "first sale" made to it by others. Contrary to petitioners' claims, this clause was not intended to preclude pipelines from recovering the NGPA incentive prices for their own production which has never been the subject of a prior first sale. As the court below properly found (App. A-8 to A-9):

> "Nothing in the language ... in the NGPA suggests any intent to deny NGPA pricing to natural gas just because it is produced by a pipeline. To the contrary, *the unless clause of subsection (B) can only have meaning if it is interpreted as granting 'first sale' status to gas which is attributable to pipeline production.*" (emphasis added).

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[11] *International Brotherhood of Teamsters v. Daniel*, 439 U.S. 551, 558 (1979). ("The starting point in every case involving the construction of a statute is the language itself.")

The Court's interpretation of "first sale" is strongly reinforced by the language of the incremental pricing provisions of the NGPA. In defining the costs which are to be passed through to certain industrial customers, Section 203(b)(1) states that the "first sale acquisition cost" of "acquired" gas shall be the "price paid." 15 U.S.C. 3343(b)(1). Following this general rule, however, is a subsection which deals specifically with "Interstate Pipeline Production", and states:

> "For purposes of this section, in the case of any natural gas *produced by any interstate pipeline* or any affiliate of such pipeline, the *first sale acquisition cost* of *such* natural gas shall be determined in accordance with rules prescribed by the Commission." 15 U.S.C. 3343(b)(2) (emphasis added).

By refering to the "first sale acquisition cost" of gas "produced by any interstate pipeline," Congress obviously envisioned that pipeline production, like production by independent producers and affiliates, would be subject to a "first sale." Otherwise, this provision would be meaningless and inoperative.[12]

The Commission and New York assert that, if Congress had intended pipeline production to qualify as a "first sale", it would not have treated pipeline production separately from other production for which there is a "price paid."[13] As the court below concluded, however:

> "This distinction ... merely reflects Congress' awareness that technically an intracorporate transfer involves no price paid. It would appear that Congress intended for the Commission to

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[12]It is an "elementary canon of construction that a statute should be interpreted so as not to render one part inoperative". *Colautti v. Franklin*, 439 U.S. 379, 392 (1979).

[13]Commission Pet. at 22-23; New York Pet. at 16.

> apply NGPA prices as the 'cost' of this gas to the pipeline, just as the Commission had applied area and national rates under the NGA to determine the 'cost' to the pipeline of pipeline produced gas." (App. A-12).

The legislative history of the NGPA also supports the lower court's finding that Congress intended the NGPA incentive prices to apply to *all* gas production by pipelines and distributors. The various committee reports and statements accompanying the NGPA reflect a widespread Congressional view that cost-based regulation under the Natural Gas Act was an "outdated mode of regulation,"[14] that it was "no longer tenable,"[15] and that it should be replaced with a uniform incentive pricing structure which applies to "any"[16] and "all"[17] gas production. Under these circumstances, and in light of the Commission's frank admission that "there is no discussion of cost-of-service pricing in the statute or in its legislative history,"[18] it is absurd for petitioners and amici to suggest that the Commission retains jurisdiction under the Natural Gas Act to regulate certain pipeline production on a cost-of-service basis.

Finally, the Commission's narrow intepretation of the NGPA is fundamentally inconsistent with the two cardinal purposes of the Act, namely, elimination of the dual market structure and establishment of economic

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[14]Statement of Rep. John Dingell, Chairman of the House Interstate and Foreign Commerce Committee, 124 *Cong. Rec.* H13114 (daily ed. Oct. 14, 1978).

[15]House Interstate and Foreign Commerce Committee, Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978, H.R. Pub. No. 95-62, 95th Cong., 2d Sess. 1-2 (1978).

[16]H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 74 (1978), *reprinted in* 1978 *U.S. Code Cong. & Ad. News*, 8983, 8991.

[17]S. Rep. No. 96-43, 96th Cong., 1st Sess. 6 (1979).

[18]Commission Pet. 20.

incentives for new exploration and development. As the court below recognized, "[n]either of these purposes is served by creating a distinction between pipeline and independent producers." (App. A-9).

With respect to the goal of establishing a single market, the court below properly found that excluding production by intrastate pipelines and local distribution companies from the NGPA pricing structure would perpetuate, rather than eliminate, the intrastate market, and would thereby leave intact "a substantial vestige of the dual market structure Congress sought to eliminate." (App. A-10). It is disingenuous for the Commission to argue that this finding is not supported by the record.[19] Indeed, one need only examine the orders in question to see that promoting state jurisdiction over certain sales of natural gas was one of the major reasons for the Commission's action (App. B-4, B-62).

It is likewise disingenuous for the Commission to suggest that its interpretation is consistent with the goal of eliminating the dual market structure because it retains discretionary authority to deal with the problem under Sections 2(21)(A)(v) and 501 of the NGPA. 15 U.S.C. 3301(21)(A)(v) and 3411.[20] That misses the point entirely. The question is not whether the Commission is vested with discretionary authority to regulate the intrastate gas market, but whether that separate market has been eliminated by Congressional mandate. On this point, there can be no doubt. As demonstrated by the legislative history of the NGPA, Congress clearly intended to abandon "the artificial distinction between the interstate and intrastate markets,"[21] and to establish

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[19]Commission Pet. 19.

[20]*Ibid.*

[21]S. Rep. No. 95-436, 95th Cong., 1st Sess. 21 (1977).

"a statutory price control formula applicable to both interstate and intrastate sales."[22]

The Commission's interpretation of "first sale" is also manifestly inconsistent with the second purpose of the NGPA, specifically, encouragement of new exploration and development. Surely, Congress did not intend to provide incentives to independent producers and affiliates, which, together produce more than 90% of the nation's gas supply (*infra*, at 27), yet simultaneously deny those incentives to pipeline producers. Congress obviously recognized, as the court below held, that, "[i]n achieving the goal of increasing natural gas production, pipeline producers deserve the price encouragement of NGPA no less than other producers." (App. A-9).[23]

Unable to deal with this facet of the court's decision on any rational legal basis, the Commission simply declares that, in its view, cost-of-service treatment has already provided pipeline producers with sufficient incentives, and they "should be entitled to no more."[24] The question below, however, was not what pipeline producers *should* be entitled to, but, rather, what *are* they entitled to, under any reasonable and logical interpretation of the NGPA. As the court of appeals stated (App. A-9):

> "The Commission's duty is to administer the law Congress passed in light of the purposes

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[22]House Interstate and Foreign Commerce Committee, Economic Analysis of H.R. 5289, *supra*, at 1-2.

[23]The Commission's failure to apply the NGPA equally to all gas production cannot be excused by the fact that the Commission, in Order No. 98, accorded the NGPA prices to certain pipeline production as a matter of discretion. As the court below emphasized, "[t]he fact that the agency gives back all or part of what it takes from the law's grant in no way justifies departure from the congressional purpose in the first instance." (App. A-9).

[24]Commission Pet. 20.

> for which it was passed. *It is not an agency's prerogative to alter a statutory scheme even if its alteration is as good or better than the congressional one.*" (emphasis added).

The Commission's rationale also ignores the fact that, historically, pipeline affiliates received precisely the same incentives as the pipelines for their cost-of-service production. Moreover, independent producers were provided with various "non-cost" incentives in the area and nationwide rates promulgated by the Commission under the Natural Gas Act.[25] If the receipt of past incentives does not preclude NGPA treatment for affiliated and independent producers, it obviously does not preclude NGPA treatment for pipeline producers.

As demonstrated above, the lower court's determination that Congress intended the NGPA to apply to all gas production is firmly rooted in the express language, legislative history, and manifest purposes of the Act. Under these circumstances, it is clear that there has been no "repeal by implication."[26]

2. Petitioners and amici also assert that an intracorporate transfer cannot be a "first sale" because it does not initially meet the legal requirements of a "sale," which is defined by Section 2(20) as "any sale, exchange, or other transfer for value."[27] 15 U.S.C. 3301(20). As common sense demonstrates, however, there must be not only a "sale", but a "first sale," at some point between the production of the pipeline's own gas and its receipt by downstream customers.

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[25]See, e.g., *Mobil Oil Corporation v. F.P.C.*, 417 U.S. 283, 316-320 (1974), where this Court upheld area rates which included various "non-cost" incentives.

[26]New York Pet. 12; Michigan Pet. 14.

[27]Commission Pet. 16; New York Pet. 16-17; Michigan Pet. 10-18; AEPCO Pet. 15-16.

While the NGPA would permit the Commission to treat the delivery to downstream customers as the point of "first sale," it also allows the Commission, as the court of appeals held, to impute a "first sale" to the point at which the pipeline transfers the gas from its production properties into the transmission system.

Contrary to the suggestions of petitioners and amici, such intracorporate transfers have significant legal and economic implications, and are clearly "transfers for value." When gas flows from the wellhead into a pipeline's interstate transmission system, it becomes subject to the full panoply of regulation under the Natural Gas Act, 15 U.S.C. 717, *et seq.*; thereafter, it cannot be transported, sold, or withdrawn from the pipeline system except as authorized by the Commission. In exchange for this transfer, the pipeline receives the right to be paid the applicable statutory price for the gas.

The legislative history of the NGPA clearly demonstrates that Congress envisioned intracorporate transfers to be both "sales" and "first sales." For example, in describing the Commission's rulemaking authority under Section 501 of the NGPA, 15 U.S.C. 3411, the House conference report states that the Commission may "establish rules applicable to *intra-corporate transactions under the first sale definition.*"[28] Petitioners argue that this statement merely indicates that the Commission has the discretion to define intracorporate transactions as "first sales," not that it is required to do so.[29] As the court below ruled, however:

> "This comment [in the report] assumes that intracorporate transactions *will* fall within the first sale definition. The decision which

[28]H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 116 (1978), *reprinted in 1978 U.S. Code Cong. & Ad. News*, 8983, 9033 (emphasis added).

[29]Commission Pet. 17, 20; New York Pet. 16.

> Congress committed to the Commission's judgment was whether regulations were necessary to govern those transactions. *The fact that the Commission was permitted to regulate intracorporate transactions under the first sale definition does not imply that Congress did not intend in the first instance for them to be treated as first sales."* (App. A-12 to A-13) (emphasis added).

Petitioners suggest that treating intracorporate transfers of pipeline production as "sales" is a "novel regulatory doctrine"[30] and a "judicially created fictional transaction."[31] As the court below recognized, however, this is precisely what the Commission itself proposed to do, as a matter of discretion, in Order No. 98. In order to allow pipelines to collect the NGPA prices for gas produced from post-1972 wells or from leases acquired after October 7, 1969, the Commission would essentially impute a "sale" at the wellhead, i.e., treat the intracorporate transfer of pipeline production as a sale by the pipeline to itself. Moreover, this is precisely what the Commission has done for the past thirteen years in permitting pipelines to value their own production from post-October 7, 1969 leases by reference to the area or nationwide rates established for independent producers. Indeed, prior to Order No. 98, the Commission's regulations relating to the flow-through of a pipeline's "purchased gas cost" stated:

> "...[P]*urchased* gas cost represents the cost of wellhead purchases, field line purchases, plant outlet purchases, transmission line purchases, *and pipeline production that qualifies for and is being afforded area or nationwide rate treatment or is otherwise being afforded rate*

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[30]Commission Pet. 14.

[31]Michigan Pet. 11.

> *treatment as though the gas were being produced by an independent producer."* (emphasis added.)[32]

Needless to say, it is fundamentally inconsistent for the Commission to treat intracorporate transfers of pipeline production as "purchased" gas and simultaneously deny that it is "sold."

Finally, there is no merit to the argument that treating an intracorporate transfer of pipeline production as a "first sale" would automatically entitle pipelines to collect the maximum NGPA ceiling prices, whereas independent producers would be limited under Section 101(b)(9), 15 U.S.C. 3311(b)(9), to the terms of their "arm's length" contracts.[33] As the court below recognized, the Commission has ample authority to impose a market limitation upon pipeline production, if it so chooses, by simply providing in its regulations that pipelines will not be allowed to exceed the highest rate charged by unaffiliated entities in comparable sales. This is exactly what the Commission has already done in Order No. 98 with respect to intracorporate transfers of gas produced by pipelines from post-1972 wells or post-October 7, 1969 leases. Specifically, the Commission has ruled that an interstate pipeline will be permitted to charge the *lower* of the NGPA rates *or* "the amount paid in comparable sales ... between persons not affiliated with such interstate pipeline or with each other." (App. B-47).

Contrary to the suggestions of petitioners and amici, the court of appeals did not hold that pipelines have superior rights to independent producers and affiliates under the NGPA. It simply ruled that all provisions of the Act — however conditioned or qualified by Congress — must be applied equally to *all* producers, not just a select majority.

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[32]18 C.F.R. 154.38(d)(4) (note 1) (1980).

[33]Commission Pet. 19-20; New York Pet. 15; Michigan Pet. 15.

3. In order to circumvent the clear meaning of the NGPA, as illuminated by its language and legislative history, petitioners and amici strenuously argue that the court below failed to give appropriate weight to alleged historical differences in the Commission's regulation of pipeline producers, vis-a-vis independent producers.[34] In this connection, it is asserted that cost-of-service regulation provided pipelines with the right to recover all prudently incurred exploration costs, including lease acquisition costs and the costs of "dry holes," and, therefore, pipeline producers were shielded from the risks traditionally borne by independent producers.[35]

The first problem with this contention is its mistaken factual premise that, historically, independent producers were not compensated for their risks. As the Commission has conceded in Order No. 98, the area and nationwide rates established for independent producers were designed "to provide for recovery of the average costs of finding, developing and producing gas *plus* an incentive *to compensate for the risks* associated with lease acquisition, exploration, and development." (App. B-25, emphasis added). Moreover, as a brief examination of the pertinent orders will demonstrate,[36] and as the Commission admits

[34]Commission Pet. 17; New York Pet. 12-13; Michigan Pet. 4-5.

[35]Commission Pet. 407, 17-18; New York Pet. 4-6, 12-13; Michigan Pet. 4-5; AEPCO Pet. 4-5.

[36]See, e.g., *Permian Basin Area Rate Proceeding*, 34 F.P.C. 159, 192, affirmed *sub nom. Permian Basin Area Rate Cases*, 390 U.S. 747 (1968). Significantly, this Court noted in *Permian* that the rate of return selected by the Commission for independent producers was based upon returns then permitted for pipelines, "but, in addition, was intended to take into account *the greater financial risks of exploration and production.*" (390 U.S. at 762, emphasis added). See, also, Commission Opinion No. 699-H, *Just and Reasonable National Rates For Sales of Natural Gas*, 52 F.P.C. 1604, 1615-16 (1974), affirmed *sub nom. Shell Oil Company* v. *F.P.C.*, 520 F.2d 1061 (5th Cir. 1976), *cert. denied*, 426 U.S. 941 (1976).

elsewhere,[37] the area and nationwide rates specifically included a component to compensate independent producers for "dry hole" costs. Under these circumstances, it is nonsensical for the Commission to attempt to justify its discrimination against pipelines by simply reasoning that pipelines have "passed on the costs of acquiring leases and the costs of exploration and development, including dry hole costs...". (App. B-27). Obviously, the same can be said about independent producers and affiliates, both of whom have been accorded NGPA treatment.[38]

Secondly, and more importantly, the Commission's argument concerning the significance of its historical treatment of cost-of-service production is refuted by its own rationale in Order No. 58. In that order, the

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[37]Commission Pet. 4.

[38]In fact, the methodology historically used by the Commission to calculate the cost-of-service for pipeline production was the same, in all material respects, as that used to calculate the area and nationwide rates for independent producers. The only significant difference was that the pipeline's cost-of-service was calculated on the basis of test-year costs for the individual company, whereas the area and nationwide rates were calculated on the basis of average industry-wide costs. While independent producers bore the risk that their return would be reduced if their actual costs exceeded the national average, they also enjoyed the right to collect a higher than average return if their individual costs were lower than the average costs. Pipeline producers had similar risks and benefits. If the pipeline producer's test-year costs exceeded average industry-wide costs, cost-of-service regulation nonetheless permitted their full recovery. On the other hand, pipeline producers, unlike independents, were not permitted to earn a larger return if their test-year costs were less than the industry-wide average. In all situations, the pipeline producer was limited to its cost-of-service, as determined on the basis of test-year costs. Moreover, in many situations, the *actual* costs incurred by the pipeline producer exceeded the *test-year* costs upon which its cost-of-service was based, thereby effectively lowering the pipeline producer's return. In short, petitioners and amici are flatly wrong in describing pipeline production as a risk-free operation.

Commission properly determined that any sale of production by an affiliate, including production formerly regulated on a cost-of-service basis, is a "first sale" which is entitled to the applicable NGPA rate (App. B-9, B-12 to B-13). The Commission also ruled that a "first sale" includes any sale of identifiable pipeline production, including production formerly regulated on a cost-of-service basis, which is contractually dedicated to a particular customer (App. B-3).

In both of these situations — affiliate sales and pipeline sales of identifiable volumes contractually dedicated to a particular customer — the production sold from pre-1973 wells on pre-October 7, 1969 leases would have the *identical* historical attributes as the pipeline production which the Commission claims should be regulated on a cost-of-service basis. Under these circumstances, it is clear that the Commission's discriminatory treatment of pipeline production is not based upon legitimate historical differences, but upon (1) the corporate *form* of the producer, and (2) the fact that most pipeline production is commingled with purchased gas prior to sale. Neither of these facts, however, can justify the Commission's interpretation of the Act. As this Court recently emphasized, statutes must be interpreted "to avoid untenable distinctions and unreasonable results whenever possible." *American Tobacco Co. v. Patterson*, No. 80-1199 (April 5, 1982), slip op. at 8.

Finally, to the extent there have been any historical differences in the regulation of certain classes or vintages of gas, such differences would not provide a rational basis for concluding that Congress intended to exclude pipeline production from the unified pricing structure of the NGPA. Indeed, the purpose of the Act was to eliminate artificial historic distinctions,[39] create a "single, national market," and put "an end to the

[39]S. Rep. No. 95-436, *supra*, at 21.

economic distortions which accompanied the outdated mode of regulation under the Natural Gas Act."[40]

4. Petitioners' last attack upon the decision below is a claim that the court of appeals failed to accord sufficient deference to the Commission's interpretation of "first sale."[41] Like their other claims, however, this contention is also without merit.

The court of appeals clearly acknowledged that the Commission's interpretation was entitled to a certain amount of deference (App. A-5). It simply refused to blindly accept an interpretation which was manifestly inconsistent with "the clear meaning of a statute as revealed by its language, purpose and history." (App. A-7). In this respect, the court's rationale was totally consistent with well-established principles of statutory construction. Indeed, as this Court recently stated, "the courts are the final authorities on issues of statutory construction," and "must reject administrative constructions of the statute ... that are inconsistent with the statutory mandate or that frustrate the policy that Congress sought to implement." *Federal Election Commission* v. *Democratic Senatorial Campaign Committee*, No. 80-939 (November 10, 1981), slip op. at 4-5; see, also, *Volkswagenwerk v. Federal Maritime Commission*, 390 U.S. 261, 272 (1968).

B. The Allegations Of Economic Impact Are Inaccurate And Provide No Basis For Review Of The Decision Below.

Several petitioners and amici speculate that according equal treatment to pipeline producers under the NGPA will precipitate significant pipeline rate increases, especially if the NGPA rates are applied

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[40]See statement of Rep. John Dingell, Chairman of the House Committee on Interstate and Foreign Commerce, 124 *Cong. Rec.* H13114 (daily ed. October 14, 1978).

[41]Commission Pet. 24; New York Pet. 11; Michigan Pet. 18.

retroactively to the effective date of the Act.[42] It is further alleged that these rate increases will result in "windfall profits" to the pipelines.[43]

These claims are largely rhetorical and are no different than those presented to Congress in the 1977-78 debates by the opponents of the NGPA. After balancing the relevant economic interests, however, Congress rejected the "windfall profits" argument, and decided that higher gas prices are necessary in order to encourage conservation and provide sufficient incentives for the development of new supplies. Thus, the court below did not decide that higher prices are appropriate as a matter of policy; it simply decided that the price structure designed by Congress was intended to apply without discrimination to *all* natural gas production.

At this point, there is not sufficient data available to meaningfully quantify the impact of applying NGPA rates to pipeline production. It is clear, nonetheless, that the projections of petitioners and amici are grossly exaggerated. AEPCO, for example, has represented that the decision below will (1) increase the price of all gas owned *or* controlled by interstate pipelines, and (2) permit NGPA prices to be applied for the first time to new wells drilled on old cost-of-service leases.[44] Neither statement is true. The Commission has already determined in Order No. 58 that all production by an affiliate, even if controlled by a pipeline, is entitled to the NGPA prices. Moreover, the Commission has already determined in Order No. 98 that the NGPA prices apply to any pipeline production which would have previously qualified for the area or nationwide rates. This includes all pipeline production from leases

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[42]Commission Pet. 15; New York Pet. 17-20; Michigan Pet. 9; AEPCO Pet. 11.

[43]Commission Pet. 20; New York Pet. 20.

[44]AEPCO Pet. 12-14.

acquired after October 7, 1969, *plus* all production from wells drilled on or after January 1, 1973, without regard to lease acquisition date. It is thus clear that the decision below impacts upon only one small category of interstate pipeline production, specifically, production from pre-1973 wells on leases acquired prior to October 8, 1969.

To place the matter in perspective, the Department of Energy statistics cited by AEPCO and New York demonstrate that approximately 92% of all gas dedicated to the major interstate pipelines in 1979 was provided by independent producers, who are undeniably entitled to the NGPA rates.[45] The remaining 8% was owned by pipelines or their affiliates. By virtue of Order Nos. 58 and 98, however, a substantial portion of this 8% would have qualified for the NGPA prices *prior to the court of appeals' decision*, because it is either (a) produced by affiliates, or (b) produced by pipelines from post-1972 wells or post - October 7, 1969 leases. Thus, the amount of production directly affected by the lower court's decision is relatively inconsequential, in comparison to the total amount of gas sold annually by the major interstate pipelines.

It must also be emphasized that the pipeline production which stands to benefit from the court's decision is on very old leases that are being rapidly depleted. As a result, the decision below will have no significant long-term impact upon national gas prices.[46]

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[45] *Statistics of Interstate Natural Gas Pipeline Companies-1979*, U.S. Department of Energy (October, 1980). See AEPCO Pet. at 12; New York Pet. at 17.

[46] At least one pipeline has taken the position that application of the NGPA price ceilings to its company-owned production would result in a *decrease* of $27.4 million in its annual revenues. See Memorandum Brief of Intervenor Northwest Pipeline Corporation (p. 3), filed with the court below on February 17, 1981.

In view of the foregoing, it is clear that the decision below does not create sufficient economic impact to justify further review by this Court. Its only significant impact is to terminate almost four years of unjustifiable pricing discrimination against a small minority of the nation's gas producers.

C. The Decision Below Does Not Conflict With The Order Of The Supreme Court Of Appeals Of West Virginia In The Pennzoil Case

Without support from the Commission, New York, or even the State of West Virginia (which filed an amicus curiae brief in this proceeding on May 12, 1982), several petitioners and amici contend that the decision below conflicts with an order issued by the Supreme Court of Appeals of West Virginia on December 10, 1981, in *Pennzoil Company v. The Public Service Commission of West Virginia*, Case No. 80-175-G-42T (W. Va. 1981) (pending before this Court on a petition for a writ of certiorari in *Pennzoil Company v. The Public Service Commission of West Virginia*, Case No. 81-1672, filed March 10, 1982).[47] Contrary to these allegations, however, there is no direct and irreconcilable conflict between the decision below and the order of the West Virginia Supreme Court of Appeals in *Pennzoil*. The one-page order in the *Pennzoil* case is nothing more than a simple denial of a petition filed by Pennzoil Company seeking review of a decision of the Public Service Commission of West Virginia.[48] The order makes no mention whatsoever of either the NGPA or the Commission's interpretation of the Act in Order Nos. 58, 98, and 102. Nor does it set forth the reasons for denying Pennzoil's petition for review.

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[47] AEPCO Pet. 13-15; Michigan Pet. 9-10.

[48] See Appendix A to Pennzoil Company's petition for a writ of certiorari in *Pennzoil Company v. The Public Service Commission of West Virginia*, No. 81-1672.

Under these circumstances, it is mere conjecture to conclude that the West Virginia Supreme Court of Appeals has interpreted "first sale," as used in the NGPA, in a manner which necessarily and irreconcilably conflicts with the decision of the court of appeals. As the Public Service Commission of West Virginia has advised the Court,[49] and as the Solicitor General and the Commission acknowledge,[50] the West Virginia Court could have denied Pennzoil's petition for appeal on several grounds which are totally unrelated to the NGPA definition of "first sale." For example, the court's disposition may have been based upon (1) a belief that states retain jurisdiction under Section 602 of the NGPA, 15 U.S.C. 3432, to establish maximum prices for in-state production which are less than the maximum NGPA ceiling prices; (2) a failure of Pennzoil to exhaust its administrative remedies; or (3) a failure by Pennzoil to show that the Public Service Commission's overall rate determination was improper under the court's standards for review. It is thus clear that there is no direct and unavoidable conflict between the decision below and the order of the West Virginia Supreme Court of Appeals in the *Pennzoil* case.

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[49]See p. 8 of Brief of the Public Service Commission of West Virginia In Opposition to Petition, filed on April 9, 1982, in *Pennzoil Company v. The Public Service Commission of West Virginia*, No. 81-1672. See, also, p. 2 of Response of Public Service Commission of West Virginia To Motion of Arizona Electric Power Cooperative, Inc., filed on April 29, 1982, in this case.

[50]In the Memorandum for the United States and the Federal Energy Regulatory Commission as Amicus Curiae, recently filed in the *Pennzoil* case, No. 81-1672, the Solicitor General has advised the Court that "there is a substantial question ... whether the judgment of the West Virginia court rests on an independent and adequate state ground." (p. 5).

CONCLUSION

For the reasons set forth above, the petitions for a writ of certiorari should be denied.

Respectfully submitted,

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August 4, 1982

Opposition

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Nos. 81-1889, 81-1958 and 81-2042

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

STATE OF MICHIGAN,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Petitions For A Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

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BRIEF IN OPPOSITION OF RESPONDENT COLORADO INTERSTATE GAS COMPANY

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QUESTION PRESENTED

Whether the United States Court of Appeals for the Fifth Circuit, upon review of Federal Energy Regulatory Commission orders, correctly interpreted that the Congressional intent embodied in the Natural Gas Policy Act of 1978 ("NGPA") was for natural gas production attributable to an "interstate' pipeline, intrastate pipeline or local distribution company, or any affiliate thereof" to be accorded first sale status under the NGPA.

LISTING OF AFFILIATES PURSUANT TO RULE 28.1

Colorado Interstate Gas Company (hereinafter "CIG"), a respondent in these cases, has previously filed herein the listing of affiliates required by Rule 28.1 of the Rules of the Supreme Court of the United States. That listing accompanied CIG's "Response In Opposition and Objection . . . To Motion Of The Public Utilities Commission Of The State Of California, Pacific Gas And Electric Company For Leave To File Brief Amici Curiae". Said "Response . . ." was dated May 19, 1982, and no amendments to it are necessary to make it currently accurate.

TABLE OF CONTENTS

	Page
Question Presented	i
Listing of Affiliates Pursuant to Rule 28.1	ii
Table of Authorities	iv
Statement of the Case	2
Summary of Argument	6
Argument	6
I. THE COURT BELOW HAS PROPERLY CONSTRUED THE NGPA	6
A. The Decision Below Does Not Result In Any Improper Repeal By Implication And In Fact That Maxim Of Statutory Construction Is Inapplicable Here	7
B. The Alleged Effects Of The Change In Commission Pricing Treatment Of Pipeline Production Which Are Asserted To Result From The Decision Below Present Neither A Basis For A Different Statutory Interpretation Nor A Reason In Equity For Review By This Court	8
II. THE DECISION BELOW DOES NOT CONFLICT WITH *PENNZOIL*	12
Conclusion	13

TABLE OF AUTHORITIES

	Page
JUDICIAL DECISIONS:	
Colorado Interstate Gas Company v. *Federal Power Commission*, 324 U.S. 581 (1945)	8,11,12
Mid-Louisiana Gas Company, et al. v. *Federal Energy Regulatory Commission*, 664 F.2d 530 (5th Cir., 1981)	*passim*
Pennzoil Company v. *Public Service Commission*, Case No. 80-175-G-42T (Sup. Ct. of Appeals of W.Va., December 10, 1981); *petition for cert. filed*, (March 10, 1982) (Case No. 81-1672)	6,12
United States v. *United Continental Tuna*, 425 U.S. 164 (1976)	8
ADMINISTRATIVE DECISIONS:	
Canadian River Gas Co., et al., 3 F.P.C. 32 (1942), *aff'd sub nom. Colorado Interstate Gas Company* v. *F.P.C.*, 324 U.S. 581 (1945)	10,11
Final Rule Governing Pricing of Pipeline Production Under the Natural Gas Act, Docket No. RM80-6, Order No. 98, issued August 4, 1980	2,3,7,9
Final Rule Governing the Maximum Lawful Price for Pipeline Distributor or Affiliate Production, Docket No. RM80-7, Order No. 58, issued November 14, 1979	2,3
Order Denying Rehearing of Order No. 58 and Order No. 98 and Clarifying Order No. 98, Docket Nos. RM80-7, RM80-6, Order No. 102, issued October 3, 1980	2,3,4
Pricing of Pipeline and Affiliate Production Under the Natural Gas Act, Docket No. RM80-6, Notice of Proposed Rulemaking, issued November 14, 1979	2

	Page
STATUTES:	
National Gas Act, 15 U.S.C. § 717, *et seq.*	3,8,11
Section 1(b), 15 U.S.C. § 717(b)	11
Section 4, 15 U.S.C. § 717(c)	8
Section 5, 15 U.S.C. § 717(d)	8
Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301, *et seq.*	*passim*
Section 2(21), 15 U.S.C. § 3301(21)	2,4,5
Section 2(21)(B), 15 U.S.C. § 3301(21)(B)	7,8
Section 602, 15 U.S.C. § 3432	13
OTHER AUTHORITIES:	
Colorado Interstate Gas Company, Federal Energy Regulatory Commission, Form No. 2, ending December 31, 1981, p. 501	12
U.S. Sup. Ct. R. 17.1	6
U.S. Sup. Ct. R. 17.1(b)	12

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1889

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

No. 81-1958

ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

No. 81-2042

STATE OF MICHIGAN,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Petitions for a Writ of Certiorari To The United States Court of Appeals For the Fifth Circuit

BRIEF IN OPPOSITION OF RESPONDENT COLORADO INTERSTATE GAS COMPANY

Colorado Interstate Gas Company (hereinafter "CIG") an intervenor below and a respondent in these cases, hereby opposes the petitions for a writ of certiorari filed by The Public Service Commission of the State of New York (hereinafter "PSC of New York") in No. 81-1889, Arizona Electric Power Cooperative, Inc. (hereinafter "AEPCO") in No. 81-1958, and the State of Michigan (hereinafter "Michigan") in No. 81-2042. PSC of New York's petition was dated April 12, 1982 and received by CIG on April 19, 1982. AEPCO's petition was dated April 22, 1982 and received by CIG on April 26, 1982. Michigan's petition, dated April 30, 1982 was received by CIG on May 6, 1982.

STATEMENT OF THE CASE

The only issue presented for review here is whether the United States Court of Appeals for the Fifth Circuit, on review of Federal Energy Regulatory Commission (hereinafter "Commission") orders, has properly interpreted the intent of Congress embodied in the Natural Gas Policy Act of 1978,[1] (hereinafter "NGPA") with respect to the pricing treatment of natural gas produced by pipelines.

In two rulemaking proceedings before the Commission[2] various parties, including CIG, argued that all pipeline produced gas should be and was intended by Congress to be treated on a full pricing parity basis with gas produced by

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[1] 15 U.S.C. § 3301, *et seq.*

[2] The Commission proceedings at Docket No. RM80-6, entitled "Pricing of Pipeline and Affiliate Production Under the Natural Gas Act" began with a "Notice of Proposed Rulemaking" issued November 14, 1979. Order No. 98, issued on August 4, 1980, promulgated the final rule in Docket No. RM80-6. The Commission proceedings at Docket No. RM80-7, entitled "Final Rule Governing the Maximum Lawful Price for Pipeline, Distributor or Affiliate Production," stem from interim regulations upon which comment was sought by order issued in November of 1978 (43 Fed. Reg. 56448, December 1, 1978). Order No. 58, issued on November 14, 1979 promulgated the final regulations interpreting Section 2(21) of the NGPA (15 U.S.C. § 3301(21)). Order No. 102, "Order Denying Rehearing of Order No. 58 and Order No. 98 and Clarifying Order No. 98," was issued in both Docket Nos. RM80-6 and RM80-7 on October 3, 1980.

others under the NGPA. The Commission, while acknowledging its authority under the NGPA to accord first sale treatment and, therefore full pricing parity to pipeline production,[3] nevertheless chose to interpret the NGPA as not applicable to pipeline production except in very limited instances.[4] The Commission determined, however, that all pipeline affiliate sales of natural gas were "first sales" under the NGPA if the affiliate is not a pipeline or distributor.[5] Pursuant to its authority under the Natural Gas Act of 1938[6] (hereinafter "NGA"), the Commission found that pipeline produced gas from wells on leases acquired by pipelines after October 7, 1969 and from wells drilled on or after January 1, 1973 on leases acquired before October 8, 1969 could be, with certain exceptions, valued by the pipelines for resale rate purposes at NGPA first sale maximum lawful ceilings.[7] The Commission found this result is both required in order to encourage the maximum production of natural gas and is consistent with the Congressional intent expressed in the NGPA.[8] Nevertheless, the Commission decided not to extend parity pricing to gas yet to be produced from pre-1973 wells on pre-October 8, 1969 leases.[9] Such gas, according to the Commission, should be priced on a cost-of-service basis since, in its view, the "equity and incentive reasons for granting parity do not apply to such gas."[10]

A number of pipeline companies sought review of the Commission's interpretation of the NGPA and its decision to not extend full pricing parity to gas produced by pipelines. Parties both in support of and opposed to the Commission's decisions intervened and participated in the United States Court of Appeals for the Fifth Circuit review proceedings.

The Fifth Circuit, in a decision evidencing full consideration of the arguments presented and a thorough analysis of

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[3] Order No. 102, (Appendix B-65).
[4] See Order No. 102, footnote 5 (Appendix B-53).
[5] Order No. 58 (Appendix B-12 and B-13).
[6] 15 U.S.C. § 717, *et seq.*
[7] Order No. 98 (Appendix B-16).
[8] Order No. 98 (Appendix B-24 through B-26).
[9] Order No. 98 (Appendix B-26).
[10] *Id.*

the statute and its legislative history and the regulatory background, found that the Commission had incorrectly determined the Congressional intent with respect to the pricing of pipeline production.[11] The Fifth Circuit summarized its holding as follows:

> Relying on the language, purposes and history of the NGPA, we hold that Congress clearly intended for any production attributable to an "interstate pipeline, intrastate pipeline or local distribution company, or any affiliate thereof" to be accorded first sale status under the NGPA and that Congress contemplated that the intracorporate transfer of pipeline production to the pipeline would be treated as the first sale. We therefore vacate Order No. 58. Because we hold that the Commission lacked authority to set prices for interstate pipeline production under the NGA, we also vacate Order No. 98 without reaching the issues of arbitrary pricing raised here.[12]

The court below outlined each of the factors which argue for greater deference to the interpretation given by an agency to its own statute, applied them to the facts of this case, and found no basis for extraordinary deference to the Commission's interpretation of the NGPA definition of "first sale".[13] The court held that neither of two "overriding purposes of the NGPA" (*i.e.*, "to eliminate the dual interstate and intrastate market for natural gas and to provide higher prices to encourage production") were "served by creating a distinction between pipeline and independent producers."[14]

Starting with the language of the statute, the court showed how the Commission's interpretation of Section 2(21) of the

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[11] Mid-Louisiana Gas Company, *et al.* v. FERC, 664 F.2d 530 (5th Cir., 1981).

[12] *Id.* at 538. (Appendix A-15); footnote citation omitted.

[13] *Id.* at 534-35. (Appendix A-7).

[14] *Id.* at 535. (Appendix A-9). The Commission in Order No. 102 found the same Congressional purposes of the NGPA (*i.e.*, "[t]he elimination of the dual market and the statutorily embraced commitment to price incentives . . .") as substantial justification for its decision to extend pricing parity to some pipeline production (Appendix B-23 through B-25).

NGPA would improperly render a portion of that statutory language a nullity and how the only way the language could have meaning would be if it was interpreted as granting "first sale" status to gas which is attributable to pipeline production.[15] The court further held that the NGPA and its relevant legislative history demonstrated that Congress intended that the intracorporate transfer of pipeline produced gas from the production division of the pipeline to the transportation division would constitute the first sale[16] and that this treatment would be consistent with and no more difficult for the Commission to administer than its present practice of treating some pipeline production as entitled to NGPA maximum lawful ceiling prices.[17]

By order issued February 5, 1982 the Fifth Circuit denied petitions for rehearing filed by PSC of New York and AEPCO and the suggestions for rehearing *en banc* of AEPCO. On March 5, 1982 the Fifth Circuit denied the motions of PSC of New York, Michigan and AEPCO for a stay of mandate pending application for a writ of certiorari.

PSC of New York, AEPCO and Michigan assert in their petitions here that the Fifth Circuit's decision must be reviewed by this Court. Largely, they cite as justification for the issuance of a writ of certiorari the same arguments of statutory construction dealt with by the court below in reaching its decision. The petitioners also assert that the *Mid-Louisiana*[18] decision will result in increased gas costs to consumers and increased revenues to pipeline producers of gas, with no requirement for "any new production effort or expense by the pipelines"[19] and cite these assertions as justifying the issuance of a writ of certiorari. Additionally, the petitions argue that the *Mid-Louisiana* decision results in an improper "repeal by implication of forty years of commission regulation of pipeline production under the Natural Gas Act."[20] Finally, the petitions state that review is

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[15] Mid-Louisiana Gas Company *et al* v. FERC, 664 F.2d at 535. (Appendix A-8 and A-9).

[16] *Id.* at 536. (Appendix A-11).

[17] *Id.* at 538. (Appendix A-14).

[18] *Id.*

[19] PSC of New York Petition, page 20.

[20] *Id.*, page 12. See also Michigan Petition, pages 14-15.

warranted by this Court because the decision below is allegedly in conflict with a decision of the highest court of a state, specifically *Pennzoil Company* v. *Public Service Commission.*[21]

SUMMARY OF ARGUMENT

The petitions for writ of certiorari should be denied. They present no "special and important reasons"[22] as to why review on writ of certiorari should be granted, and, in fact, no such reasons exist. The issue presented for review is one of statutory construction which has been carefully and thoroughly examined by the court below within the context of established principles of judicial review. The decision does not result in any "repeal by implication," and it is doubtful whether the principle of "repeal by implication" is applicable here. The asserted effect of the decision below, specifically increased revenues to pipeline producers of gas, is exactly what Congress intended by enactment of the NGPA to encourage the maximum production of natural gas and should not be a reason for issuance of a writ of certiorari. Finally, the decision below plainly does not conflict with the *Pennzoil* decision.

ARGUMENT

I. The Court Below Has Properly Construed The NGPA.

The *Mid-Louisiana* opinion evidences that the Fifth Circuit carefully considered and dealt with each of the arguments of statutory construction raised by the petitioners here. Contrary to the assertion of the PSC of New York (Petition, page 11), the Fifth Circuit gave the Commission's interpretation of the NGPA the deference it was due. Likewise the court correctly

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[21] Case No. 80-175-G-42T, December 10, 1981. The decision is not reported. A petition for writ of certiorari in this matter was filed on March 10, 1982 in No. 81-1682. The decision is reproduced in the Appendix to Petition for a Writ of Certiorari in No. 81-1672.

[22] Rule 17.1, Rules of the Supreme Court of the United States.

held that no "bizarre" results[23] would stem from its reading of the statute since the Commission is already treating some pipeline produced gas as if sold at the wellhead for NGPA first sale maximum lawful ceilings.[24] On the contrary, the court noted that the Commission's reading of the statute would have the truly bizarre result of reading out of the statute the "unless" clause of Section 2(21)(B) of the NGPA.[25] That is the result clearly sought by the petitioners. They, for all practical purposes, urge this Court to reverse the Fifth Circuit and hold that Congress intended that there can be no "first sale" of the vast majority of the gas produced by pipelines and sold by them to their distribution customers for resale to end users. The court below, CIG submits, has convincingly demonstrated that this result is supported by neither the express statutory language nor the legislative history of the NGPA. There is no compelling reason to overturn this decision of the Fifth Circuit.

A. The Decision Below Does Not Result In Any Improper "Repeal By Implication" And In Fact That Maxim Of Statutory Construction Is Inapplicable Here.

PSC of New York and Michigan assert in their petitions, at pages 12 and 15, respectively, that the decision of the court below results in an improper "repeal by implication" of "forty years of commission regulation of pipeline production under the Natural Gas Act."[26] This argument is unconvincing upon closer review.

The maxim against statutory repeals by implication does not apply to repeal by later statute of the type of discretionary agency practice involved here. Instead, the maxim against

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[23] PSC of New York Petition, page 15; Michigan Petition, page 19; AEPCO Petition, pages 17-18.

[24] Mid-Louisiana Gas Company, *et al.* v. FERC, 664 F.2d at 538, (Appendix A-14).

[25] 15 U.S.C. § 3301(21)(B). Michigan's assertion that there are many sales by pipelines at the wellhead to other pipelines and end users which would be treated as first sales under the Commission's interpretation of the NGPA (Petition, pages 18-19) is totally unsupported by the record. The Commission said in Order 98 that only a "limited amount" of pipeline production would be covered. (Appendix B-19).

[26] PSC of New York Petition, page 12.

statutory repeals by implication is to preclude nullification of specific policy judgments made by Congress in an earlier act. *United States* v. *United Continental Tuna,* 425 U.S. 164 at 169, 181 (1976). Congress did not specify in the NGA how the Commission should value pipeline production in approving or fixing rates under Sections 4 and 5 thereof. *Colorado Interstate Gas Company* v. *Federal Power Commission,* 324 U.S. 581, 601-604 (1945). The "unless" clause of Section 2(21)(B) of the NGPA[27] is the first statutory expression of Congressional intent as to the pricing of pipeline production.

Additionally, the "unless" clause of Section 2(21)(B) expressly states the Congressional intention regarding the "first sale" status of all transfers of pipeline produced gas. Therefore, even if the maxim of repeal by implication applied to "repeals" of discretionary agency practice, it could not apply here because Congress expressly intended that pipeline production be priced as "first sales."

B. The Alleged Effects Of The Change In Commission Pricing Treatment Of Pipeline Production Which Are Asserted To Result From The Decision Below Present Neither A Basis For A Different Statutory Interpretation Nor A Reason In Equity For Review By This Court.

The petitioners paint the decision below as mandating a radical departure in long-standing Commission regulatory practice. They say this change will result in increased gas costs to consumers and increased revenues to pipeline producers of natural gas with no requirement for new production efforts by those pipeline producers. They claim Congress cannot have intended these results and that the court below was wrong to infer them. The petitioners also imply that the mere size of the resulting increased costs to consumers warrants review. They further argue that "[p]ipelines have not had to bear the risks of production and should not receive the gain associated within NGPA prices, especially when they earlier elected cost-of-

[27] *Supra,* note 25.

service pricing because it was then beneficial."[28] None of these arguments withstand closer scrutiny.

Contrary to petitioners' assertions, the record demonstrates that since 1969 the Commission and its predecessor, the Federal Power Commission, have been committed to the policy of parity pricing for pipeline and pipeline affiliate production.[29] Only gas from wells drilled before January 1, 1973 on leases acquired by pipelines prior to October 8, 1969 was continued to be priced on a cost-of-service basis after that date and even the petitioner, PSC of New York, recognizes that under this policy such "old" cost-of-service priced gas would decline as those wells depleted.[30] It is reasonable to assume, given the Congressional purposes embodied in the NGPA of increasing incentives for maximizing the production of natural gas, that Congress acted by the NGPA to accelerate the ultimate end of previously established Commission policy on the pricing of pipeline production.

There is no dispute between the court below and the Commission that one of the purposes of the NGPA included the establishment of increased incentives for the production of natural gas. This purpose could not have been implemented without a resulting increase in the cost of gas to consumers. Congress recognized this result and provided a mechanism intended to reduce its effect on certain end-users by the incremental pricing provisions in Title II of the NGPA. There was no requirement in the NGPA for any producers of gas to undertake new production efforts in order to qualify for NGPA authorized ceiling prices for both new and flowing gas. Congress instead assumed natural gas producers would act rationally to these additional incentives by increasing their exploration for and production of natural gas. Thus, the successful attainment of a central purpose and anticipated result of the NGPA, *i.e.* increased revenues to producers of gas, cannot legitimately be asserted by petitioners as a reason for review and reversal by this Court of the decision below.

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[28] Michigan Petition, page 15.

[29] Order No. 98, (Appendix pages B-21 and B-22).

[30] PSC of New York Petition, page 19.

Since Congress left no doubt it was aware that increased gas costs to consumers would result from enactment of the NGPA, that fact does not require the issuance of a writ of certiorari here. In any event, petitioners have not accurately described those increased costs.[31] Neither have the petitioners proven that increased consumer costs will result from the decision below. Rather than resulting in increased costs to gas consumers, the effect of the Fifth Circuit decision could just as likely be a redistribution of revenues among producers with no resultant change in consumer costs. Furthermore, it might be reasonably assumed that increased gas production by pipelines would result from the incentives included in the NGPA and such additional gas will be available to end users to offset more expensive alternate fuels.

Finally, the argument that Congress could not have intended to permit pipelines to gain from the passage of NGPA since those pipelines "elected" to have their risks of production borne by their resale customers is absurd. Any such Congressional intent is neither expressed nor implied in the NGPA or its legislative history. Quite a contrary factual history is evidenced with respect to CIG in the cases cited by both PSC of New York and AEPCO as establishing the history of cost-of-service pricing for pipeline production. Those cases are *Canadian River Gas Co. et al.*, 3 F.P.C. 32 (1942), *aff'd. sub nom.*,

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[31] For example, both PSC of New York and Michigan state that CIG has submitted a general rate increase reflecting a $104,618,064 retroactive cost increase because of the decision below and a $22,948,093 prospective annual increase. (PSC of New York Petition, page 18 and Michigan Petition, page 9). The correct figures for increases to CIG's jurisdictional customers included in the subject filing are approximately $88.8 million (for the retroactive period) which CIG proposes to collect over a three year period and $19.8 million (for the prospective annual periods). Additionally, AEPCO's attempt to quantify the effect of the decision below at page 13 of its petition by saying "Each $1 difference in this price equals $12.4 billion dollars [sic] over the life of these gas reserves", is obviously incorrect. Among other things, AEPCO did not eliminate from the 12.4 billion cubic feet of pipeline owned reserves it found in 1979 the pipeline owned gas which would be entitled to NGPA first sale pricing under Commission regulations existing prior to the decision by the Fifth Circuit below.

Colorado Interstate Gas Company v. *FPC*, 324 U.S. 581 (1945). The cases reveal that Canadian River, an affiliate of CIG at that time which was subsequently merged into CIG, acquired its gas production properties in the Texas Panhandle[32] in 1928,[33] fourteen years before the Commission announced in the *Canadian River* case that such production must be priced on a cost-of-service basis and ten years before the enactment of the Natural Gas Act. No one can say CIG and its predecessors undertook to explore for and develop the gas on these properties in recognition that the risks attendant thereto would be underwritten by Commission pricing policy.

Likewise, no one can legitimately argue that CIG and its predecessors "elected" cost-of-service treatment for its own production. To the contrary, Canadian River contended the regulation of its production was beyond the Commission's jurisdiction under Section 1(b) of the NGA.[34] As to the pricing of such gas, this Court summarized Canadian River's argument as follows:

> It is argued that the correct procedure is for the Commission to allow in the operating expenses of a natural-gas company, whose rates it is empowered to fix, the "fair field price" or "fair market value, as a commodity, of the gas" which finds its way into the transmission lines for interstate transportation and sale.[35]

This Court did not accept Canadian River's argument and instead affirmed the Federal Power Commission decision below to price Canadian River's pipeline production on a cost-of-service basis. In making its decision this Court stated its reasoning as follows:

> Congress of course might have provided that producing or gathering facilities be excluded from the rate base and that an allowance be made in operating expenses for the fair field price of the gas as a

---

[32] CIG's Texas Panhandle properties still supply approximately 94% of CIG's company-owned pipeline production.

[33] Colorado Interstate Gas Company v. FPC, 324 U.S. at 584.

[34] 15 U.S.C. 717(b).

[35] Colorado Interstate Gas Company v. FPC, 324 U.S. at 600.

> commodity. Some have thought that to be the wiser course. But we search the Act in vain for any such mandate.[36]

The court below has correctly read the NGPA as stating the Congressional mandate for which this Court searched in *Colorado Interstate*.[37]

II. The Decision Below Does Not Conflict With *Pennzoil*.

AEPCO and Michigan assert that *Mid-Louisiana* and *Pennzoil*[38] are related and in conflict and contend that a writ of certiorari, therefore, must issue under Rule 17.1(b) of the Rules of the Supreme Court of the United States. As this Court is aware, Rule 17.1(b) does not mandate review in the instance then described. In any event the one page order of the Supreme Court of Appeals of the State of West Virginia in *Pennzoil* merely affirmed a decision of the Public Service Commission of West Virginia. The court order revealed absolutely no basis for its decision, much less a basis in conflict with the decision in *Mid-Louisiana*. Furthermore, the PSC of West Virginia decision affirmed by the state court expressed bases for the result reached which are completely independent of the *Mid-Louisiana* interpretation of the NGPA.

The "Response of the Public Service Commission of West Virginia to the Motion of Arizona Electric Power Cooperative, Inc., For Contemporaneous Consideration and Disposition of Petitions For Certiorari" dated April 29, 1982 and filed in No. 81-1958 reaffirms that no conflict exists between *Mid-Louisiana* and *Pennzoil*. Further, in its brief in opposition to the petition for a writ of certiorari in No.81-1672 the PSC of West Virginia

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[36] *Id.*, at 601.

[37] The legacy of cost-of-service pricing of pipeline produced gas is demonstrated by comparing the amount of gas producing properties owned by Canadian River in December of 1939 (approximately 300,000 acres) and the lesser amount of gas producing properties owned by CIG today (approximately 268,423 acres). Colorado Interstate Gas Company v. FPC, 324 U.S. at 585; CIG Federal Energy Regulatory Commission, Form No. 2, year ending December 31, 1981, page 501.

[38] *Supra*, note 21.

states independent bases upon which the state court could have relied in affirming the agency decision. Briefly those bases are:

(a) The reservation of state jurisdiction over intrastate gas production by Section 602 of the NGPA,[39]

(b) The failure of Pennzoil to exhaust its administrative remedies (Pennzoil failed to apply for rehearing of the Commission order), and

(c) Pennzoil's failure to show that the PSC of West Virginia's overall rate determination was improper under the state court's standard of review.

The facts are convincing, CIG submits, that no conflict between the two decisions exists, and there is no compelling reason for this Court to search for one.

CONCLUSION

The petitions for a writ of certiorari should be denied, since they present no special and important reasons for review by this Court.

Respectfully submitted,

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[39] 15 U.S.C. § 3432 (a).

Opposition

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Nos. 81-1889, 81-1958, 81-2042, 82-19

IN THE

Supreme Court of the United States

October Term, 1982

The Public Service Commission Of The State Of New York, *et al.*,

Petitioners,

v.

Mid Louisiana Gas Company, *et al.*,

Respondents.

On Petitions For A Writ of Certiorari To The United States Court of Appeals For The Fifth Circuit

---

BRIEF OF RESPONDENT CONSOLIDATED GAS SUPPLY CORPORATION IN OPPOSITION

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QUESTION PRESENTED

Whether the Fifth Circuit was correct when it ruled that the Federal Energy Regulatory Commission does not have the statutory authority to preclude interstate pipelines, intrastate pipelines, and local distribution companies from receiving the Natural Gas Policy Act's incentive prices for their natural gas production.

TABLE OF CONTENTS

PAGE

QUESTION PRESENTED i

TABLE OF CONTENTS ii

TABLE OF AUTHORITIES iii

ADDITIONAL STATUTORY PROVISIONS 2

STATEMENT OF THE CASE 4

SUMMARY OF ARGUMENT 5

ARGUMENT 6

I. The Decision Of The Fifth Circuit Is Fully Supported By The Statute And Its Legislative History 6

II. The Decision Of The Fifth Circuit Neither Established A Novel Regulatory Doctrine Nor Overturned Forty Years Of Regulatory History 11

III. The Economic Impact Of Section 2(21)(B) Of The Natural Gas Policy Act Is Not Relevant To Its Interpretation 15

IV. The Decision Of The Fifth Circuit Does Not Conflict With The "Decision" Of The West Virginia Supreme Court 16

CONCLUSION 18

TABLE OF AUTHORITIES

CASES	PAGE
Baker v. Carr, 369 U.S. 186 (1962)	15
Conoco, Inc. v. FERC, 622 F.2d 796 (5th Cir. 1980)	8, 15
Ecee, Inc. v. FERC, 611 F.2d 554 (5th Cir. 1980)	8
Kansas-Nebraska Natural Gas Co., 53 F.P.C. 1691 (1975)	13
Monrosa v. Carbon Black Export, Inc., 359 U.S. 180 (1959)	17
Opinion No. 699-H, Just and Reasonable National Rates for Sales of Natural Gas, 52 F.P.C. 1604, *aff'd sub nom. Shell Oil Co. v. FPC*, 520 F.2d 1061 (5th Cir.) *cert. denied*, 426 U.S. 941 (1975)	12
Opinion No. 770, National Rates for Jurisdictional Sales of Natural Gas, 56 F.P.C. 509 (1976), *aff'd sub nom. American Public Gas Ass'n v. FPC*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978)	12
Pennzoil Co. v. FERC, 645 F.2d 360 (5th Cir. 1981), *cert. denied*, 102 S. Ct. 1000 (1982)	15
Pennzoil Co. v. Public Service Comm'n of W. Va., No. 80-175-G-42T (Jan. 18, 1982), *petition for cert. filed*, 50 U.S.L.W. 3768 (U.S. March 10, 1982) (No. 81-1672)	6, 17
Permian Basin Rate Proceeding, 34 F.P.C. 159 (1965), *aff'd*, 390 U.S. 747 (1968)	11

Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672 (1954) 11

Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738, *modified*, 42 F.P.C. 1089 (1969), *aff'd sub nom. City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (19[illegible]) 12

STATUTES

Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-3432 (Supp. IV 1980) ..... *passim*

§ 2(21), 15 U.S.C. § 3301(21) (Supp. IV 1980) ... 8
§ 102(c), 15 U.S.C. § 3312(c) (Supp. IV 1980) .. 11
§ 103(c), 15 U.S.C. § 3313(c) (Supp. IV 1980) .. 11
§ 107(c), 15 U.S.C. § 3317(c) (Supp. IV 1980) .. 11
§ 203, 15 U.S.C. § 3343 (Supp. IV 1980) 9
§ 601, 15 U.S.C. § 3431 (Supp. IV 1980) .. 8, 9, 10

MISCELLANEOUS

124 Cong. Rec. H13114 (daily ed. Oct. 14, 1978) 15

H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. (1978) 10

Regulations Implementing Section 110 of the Natural Gas Policy Act of 1978 and Establishing Policy Under the Natural Gas Act, Order No. 94, Docket No. RM80-47 (Issued July 25, 1980) 7

S. Rep. No. 95-1126, 95th Cong., 2d Sess. (1978) ... 9

Nos. 81-1889, 81-1058, 81-2042, 82-19

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On Petitions For A Writ of Certiorari To The United States Court of Appeals For The Fifth Circuit

---

BRIEF OF RESPONDENT CONSOLIDATED GAS SUPPLY CORPORATION IN OPPOSITION

Respondent Consolidated Gas Supply Corporation[1] respectfully requests that this Court deny the petitions for writ of certiorari seeking review of the Fifth Circuit's opinion in this case filed by the Public Service Commission of the State of New York in No. 81-1889, Arizona Electric Power Cooperative, Inc. in No. 81-1958, the State of Michigan in No. 81-2042, and the Federal

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[1]Consolidated Gas Supply Corporation is a wholly-owned subsidiary of Consolidated Natural Gas Company. Consolidated Gas Supply Corporation is an affiliate of Consolidated Natural Gas Service Company, Inc., The East Ohio Gas Company, The Peoples Natural Gas Company, West Ohio Gas Company, The River Gas Company, CNG Producing Company, Consolidated System LNG Company, CNG Development Company, Ltd., CNG Research Company, and CNG Coal Company.

Energy Regulatory Commission in No. 82-19. The Fifth Circuit's opinion is reported at 664 F.2d 530. None of the petitions articulate any special or important reason for granting a writ of certiorari. The decision of the Fifth Circuit resolves a question of statutory construction and raises no new or novel issue, involves no constitutional question, and creates no conflict with any decision of this Court or any other court.

ADDITIONAL STATUTORY PROVISIONS

Sections 601(a)(1)(A) and (B) of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3431(a)(1)(A) and (B) (Supp. IV 1980), provide:

> § 3431. COORDINATION WITH THE NATURAL GAS ACT
>
> (a) Jurisdiction of the Commission under the Natural Gas Act
>
> (1) Sales
>
> (A) Natural gas not committed or dedicated
>
> For purposes of section 1(b) of the Natural Gas Act [15 U.S.C. 717(b)], effective on the first day of the first month beginning after November 9, 1978, the provisions of the Natural Gas Act [15 U.S.C. 717 et seq.] and the jurisdiction of the Commission under such Act shall not apply to natural gas which was not committed or dedicated to interstate commerce as of November 8, 1978, solely by reason of any first sale of such natural gas.
>
> (B) Committed or dedicated natural gas
>
> Effective beginning on the first day of the first month beginning after November 9, 1978, for purposes of section 1(b) of the Natural Gas Act [15 U.S.C. 717(b)], the provisions of such Act [15 U.S.C.

717 et seq.] and the jurisdiction of the Commission under such Act shall not apply solely by reason of any first sale of natural gas which is committed or dedicated to interstate commerce as of November 8, 1978, and which is —

(i) high-cost natural gas (as defined in section 3317(c)(1), (2), (3), or (4) of this title);

(ii) new natural gas (as defined in section 3312(c) of this title); or

(iii) natural gas produced from any new, onshore production well (as defined in section 3313(c) of this title).

Sections 601(b) and (c), 15 U.S.C. §§ 3431(b) and (c) (Supp. IV 1980), provide, in pertinent part:

(b) Charges deemed just and reasonable

(1) Sales

(A) First sales

Subject to paragraph (4), for purposes of sections 4 and 5 of the Natural Gas Act [15 U.S.C. 717c, 717d], any amount paid in any first sale of natural gas shall be deemed to be just and reasonable if —

(i) such amount does not exceed the applicable maximum lawful price established under subchapter 1 of this chapter; or

(ii) there is no applicable maximum lawful price solely by reason of the elimination of price controls pursuant to part B of subchapter 1 of this chapter.

***

(c) Guaranteed passthrough

***

(2) Recovery of just and reasonable prices paid

For purposes of sections 4 and 5 of the Natural Gas Act [15 U.S.C. 717c, 717d], the Commission may not deny any interstate pipeline recovery of any amount paid with respect to any purchase of natural gas if —

(A) under subsection (b) of this section, such amount is deemed to be just and reasonable for purposes of sections 4 and 5 of such Act [15 U.S.C. 717c, 717d], and

(B) such recovery is not inconsistent with any requirement of any rule under section 3341 of this title (including any amendment under section 3342 of this title),

except to the extent the Commission determines that the amount paid was excessive due to fraud, abuse, or similar grounds.

***

STATEMENT OF THE CASE

The Natural Gas Policy Act of 1978 ("NGPA")[2] establishes a uniform national pricing scheme applicable to all "first sales" of domestic natural gas production. (App. D-1). In its Order No. 58, interpreting the term "first sale", and in its regulations implementing the NGPA, the Federal Energy Regulatory Commission ("Commission") ruled that there could be no "first sale" of natural gas produced by an interstate pipeline, intrastate pipeline, or local distribution company, unless the sale was comprised exclusively of that company's production. (App. B-5). The Commission recognized that, because virtually all pipeline or local distribution company production becomes a part of system supply and is commingled with gas purchased from other sources prior to sale, its order effectively

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[2] 15 U.S.C. §§ 3301-3432 (Supp. IV 1980). References to Appendix cites refer to the Appendix to the petition in No. 81-1889.

precluded pipelines and distributors from receiving NGPA incentive prices for their own production. (App. B-3).

Having concluded that virtually all sales of pipeline and distributor production did not qualify as "first sales" under the NGPA, the Commission promulgated a rulemaking under the Natural Gas Act ("NGA"), Order No. 98, establishing the prices at which it would permit natural gas produced by interstate pipelines to be sold. (App. B-16).

The court below vacated the Commission's Order No. 58 and held that Congress clearly intended the "first sale" of *all* domestic natural gas production, whether produced by an independent producer, an interstate pipeline, an intrastate pipeline, a local distribution company, or any affiliate thereof, to qualify for the NGPA incentive prices. (App. A-15). As a result of this holding, the court necessarily vacated Order No. 98, the continued effectiveness of which was dependent upon the validity of Order No. 58.

SUMMARY OF ARGUMENT

The Court should deny the petitions, no special or important reason for granting a writ of certiorari having been articulated:

1. The Fifth Circuit carefully examined the language, purpose, and legislative history of the NGPA and properly held that Congress intended Title I of the NGPA to apply to the first sale of *all* domestic natural gas production, including natural gas produced by pipelines, local distribution companies and their affiliates, and that the Commission must devise appropriate regulations to carry out Congress' intent;

2. The Fifth Circuit did not establish a novel regulatory doctrine nor did it overturn more than forty years of regulatory policy;

3. The economic impact of an Act of Congress is not relevant where the only issue before the Court is whether the act is properly interpreted; and

4. No conflict exists between the Fifth Circuit's decision and the decision of the West Virginia Supreme Court in *Pennzoil Co. v. Public Service Comm'n of W. Va.*, Case No. 80-175-G-42T, now before this Court on Petition For A Writ of Certiorari in No. 81-1672.

ARGUMENT

I. The Decision Of The Fifth Circuit Is Fully Supported By The Statute And Its Legislative History

The Fifth Circuit held:

> Relying on the language, purposes and history of the NGPA, we hold that Congress clearly intended for any production attributable to an "interstate pipeline, intrastate pipeline or local distribution company, or any affiliate thereof" to be accorded first sale status under the NGPA and that Congress contemplated that the intracorporate transfer of pipeline production to the pipeline would be treated as the first sale.

(App. A-15). Explaining its holding, the court commented: "The effect of our holding with respect to Order No. 58 is that the price for pipeline production will now be set under the NGPA." (App. A-15, n.4).

The second part of the court's holding — that first sale treatment of intracorporate transfers was contemplated by Congress — is not a mandate requiring the Commission to adopt any particular method of applying Title I to those transfers. In this portion of its holding the court was responding to the litany of administrative "difficulties" the Commission argued it would encounter were it to recognize the first sale of pipeline production when it actually took place — downstream, after commingling:[3]

> Although the legislative history convinces us that Congress intended the intracorporate transfer to be treated as a first sale, we respect the Commission's determination that administration would be difficult. We note, however, that in Order No. 98 the Commission would apply NGPA prices to this same intracorporate transfer. This assures us that the Commission's authority to issue regulations to govern this area will enable it to overcome these difficulties.[4]

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[3]Contrary to the statement in the Commission's petition at p. 15, the court did not agree with the Commission that the term "first sale" was intended to encompass only sales from the field or well-head, and not "downstream" sales of a pipeline producer from system supply. For the Commission to suggest to this Court that "downstream" sales were not intended to be included within the term "first sale" is, at a minimum, surprising in view of the Commission's admission in Order No. 58 that such sales may be first sales (App. B-3) and its statement in its rulemaking implementing NGPA section 110 (production-related costs):

> Thus, the Congress provided that first sale ceiling prices may apply downstream from the wellhead, and that they would apply "at the wellhead".

Regulations Implementing Section 110 of the Natural Gas Policy Act of 1978 and Establishing Policy Under the Natural Gas Act, Order No. 94, Docket No. RM80-47, mimeo at 15 (Issued July 25, 1980). The Fifth Circuit recognized as much. (App. A-10).

[4]App. A-14.

On its face, the statute includes within the definition of the term "first sale" sales of pipeline, distributor and affiliate production. Section 2(21)(B) merely eliminates from the definition of the term "first sale" resales by pipelines and distributors of natural gas purchased from others. This exception to the "first sale" definition does not, however, exclude initial sales by pipelines and distributors of their own production. As the Fifth Circuit correctly stated, the purpose of this exception to the all-inclusive first sale definition was to eliminate second first sales by pipelines or local distribution companies of gas purchased from others. A pipeline could not, then, buy natural gas in a first sale and resell it in another first sale. (App. A-8). However, to the extent that a pipeline's sales are attributable to its own production, they are first sales controlled by Title I of the NGPA.

The statute's meaning is plain. Congress establishes maximum lawful prices under the NGPA for the first sale of all domestic production; but the Commission remains free under the NGA to determine and fix just and reasonable rates for all volumes of natural gas that are resold by pipelines in interstate commerce. The Commission's NGA jurisdiction over resales is affected only by the requirement that the Commission permit full recovery of congressionally-established applicable NGPA prices.[5]

The plain meaning of a statute controls, except where the interpretation would lead to an absurd result or a result contrary to the policy of the legislation taken as a whole. *Ecee, Inc. v. FERC*, 611 F.2d 544, 561 (5th Cir. 1980). Here, the definition is clear, *Conoco, Inc. v. FERC*, 622 F.2d 796, 798 (5th Cir. 1980), and the result reached is completely consistent with the legislation when read as a whole.

---

[5]NGPA § 601(c), 15 U.S.C. § 3431(c) (Supp. IV 1980).

For example, in NGPA section 203, Congress directed the Commission to prescribe rules to determine the "first sale acquisition cost" of any natural gas produced by an interstate pipeline. (App. D-3). NGPA section 203(b)(2) reads:

> (2) Interstate pipeline production. —
> For purposes of this section, in the case of any natural gas produced by an interstate pipeline or any affiliate of such pipeline, the first sale acquisition cost of such natural gas shall be determined in accordance with rules prescribed by the Commission.

Had Congress intended to exclude the sale of a pipeline's production from qualifying as a first sale it would not have made specific reference to pipeline production as a first sale.

Congress simply directed the Commission to prescribe rules to determine the first sale acquisition cost in full recognition of the fact that the first sale price could not be determined by reference to an arms-length contract price. Thus, the Commission was to prescribe rules here much in the same way that it was to prescribe rules dealing with the application of the first sale definition to intracorporate transfers of pipeline production. As Congress instructed the Commission:

> [T]he Commission ... may ... establish rules applicable to intracorporate transactions under the first sale definition.[6]

Congress did not leave the Commission without guidance in this regard. In NGPA section 601(b)(1)(E) it established an objective standard against which

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[6]S. Rep. No. 95-1126, 95th Cong., 2d Sess. at 116 (1978).

intercorporate "first sales" between affiliates would be measured. (App. D-4). Although this section does not specifically reference intracorporate transfers, the Commission may use this same standard in promulgating rules on intracorporate transfers. However, as the court below held, the Commission may not refuse to recognize the first sale of the pipeline's production either at the wellhead or at some downstream point.[7]

Other statutory provisions also fully support the court's interpretation of Congress' intent. NGPA section 601(a)(1)(A) excludes from the Commission's NGA jurisdiction the sale for resale in interstate commerce of natural gas not committed or dedicated to interstate commerce as of November 8, 1978. Under the Commission's view of the NGPA, NGA jurisdiction would be retained over the sale for resale of natural gas if it were produced by interstate pipelines. Congress never intended that result:

> Natural gas not committed or dedicated to interstate commerce as of the day before the date of the enactment of this Act is *never* made subject to the Commission's jurisdiction under sec. 1(b) of the Natural Gas Act.[8]

Additionally, section 601(a)(1)(B) excludes from the Commission's jurisdiction, effective December 1, 1978,

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[7]The Commission did exactly what Congress contemplated when it applied the NGPA section 601(b)(1)(E) affiliated entities rule to intracorporate transfers of pipeline production in Order No. 98. *See* App. B-36.

[8]H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. at 123 (1978) (emphasis added).

high-cost natural gas which qualifies under section 107(c)(1), (2), (3), or (4); new natural gas which qualifies under section 102(c); and natural gas produced from any new, onshore production well which qualifies under section 103(c). As to these categories of natural gas the conferees stated:

> The Commission's jurisdiction under section 1(b) of the Natural Gas Act ceases on the first day of the first month beginning after the date of enactment of this Act ....[9]

As the Fifth Circuit held, the result urged by petitioners here contravenes the plain meaning of the statute and is inconsistent with its fundamental purposes. (App. A-9).

II. The Decision Of The Fifth Circuit Neither Established A Novel Regulatory Doctrine Nor Overturned Forty Years Of Regulatory History

Prior to the enactment of the NGPA, the price of all domestic natural gas that was produced and sold in the interstate market was regulated by the Federal Energy Regulatory Commission or its predecessor, the Federal Power Commission. Until the Commission issued its order in the first area rate proceeding in 1965, all natural gas production subject to the Commission's NGA jurisdiction was priced on a company-by-company cost-of-service basis.[10] Subsequently, all natural gas produced by independent producers was priced on an

---

[9] *Id.*

[10] Independent producers became subject to the Commission's NGA jurisdiction following this Court's decision in *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672, 685 (1954). The Commission's first area rate order was issued in *Permian Area Rate Proceeding*, 34 F.P.C. 159 (1965), *aff'd*, 390 U.S. 747 (1968).

area or nationwide basis.[11]

With respect to natural gas produced by interstate pipelines, however, the Commission continued cost-of-service pricing until 1969. On October 7, 1969, the Commission determined that, to encourage drilling, pipelines should be treated in parity with independent producers. Accordingly, in Opinion No. 568, the Commission permitted pipelines to receive area rates for all gas produced on leases acquired after October 7, 1969.[12] The Commission later extended parity to all natural gas produced by pipelines from wells drilled after January 1, 1973, regardless of the lease acquisition date.[13]

With respect to pipeline production priced under area or nationwide rates, the Commission imputed a value to the gas at the point of transfer from the pipeline's production operation to its transmission operation in calculating the pipeline's rates to its customers. As the Commission explained:

> Although the pipeline production was not acquired in a sale and no certificates were issued for the pipeline's acquisition of its own

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[11]Opinion No. 699-H, Just and Reasonable National Rates for Sales of Natural Gas, 62 F.P.C. 1604, *aff'd sub nom.* Shell Oil Co. v. FPC, 520 F.2d 1061 (5th Cir.), *cert. denied,* 426 U.S. 941 (1975); Opinion No. 770, National Rates For Jurisdictional Sales of Natural Gas, 56 F.P.C. 509 (1976), *aff'd sub nom.* American Public Gas Ass'n v. FPC, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied,* 435 U.S. 907 (1978).

[12]Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738, modified, 42 F.P.C. 1089, 1091, *aff'd sub nom.* City of Chicago v. FPC, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied,* 405 U.S. 1074 (1972).

[13]See note 11, *supra.*

> production, the Commission allowed the value for such gas, determined by reference to area or nationwide rates, to be reflected in the pipeline's semi-annual purchased gas filings and passed through to purchasers on the same basis as natural gas purchased from producers. 18 C.F.R. § 154.38(d)(4), note 1.[14]

Thus, as the court below properly observed:

> The Commission treated the pipeline's intracorporate transfer of its own production as if it had been bought from another entity and determined its "cost" to the pipeline applying the same area or national rates the Commission applied to independently produced gas.[15]

It is disingenuous for petitioners to suggest that the Fifth Circuit established a "novel regulatory doctrine" when it found that the continuation and extension of the Commission's then-current practice of imputing ceiling prices to intracorporate pipeline transfers was within the contemplation of Congress when it enacted the NGPA.

Equally without merit is petitioner's argument that over forty years of regulatory history (*i.e.*, cost-of-service regulation of pipeline production) has been overturned by the court's decision. If forty years of history had been overturned, it would not have been overturned by the court; it would have been

[14]App. B-55, n. 9. The only exception to this pricing scheme was the opportunity for the pipeline producer to prove that special circumstances justified prices over and above the area or nationwide rate set by the Commission. The Commission was clear, however, that a pipeline's inability to recover its expenditures and earn the allowed return on production would not constitute special circumstances. See Kansas-Nebraska Natural Gas Co., 53 F.P.C. 1691, 1696-99 (1975).

[15]App. A-2.

overturned by Congress. However, Congress did not overturn history; it merely hastened the demise of cost-of-service pricing of pipeline production. The Commission itself acknowledged this trend away from cost-of-service pricing in Order No. 98:

> Having embarked under the NGA upon a course which would provide price incentives for both pipeline and independent producer production to encourage production of additional gas supplies, and having been reaffirmed in this course by evidence of a similar purpose in Congress' enactment of a pricing scheme in the NGPA designed to encourage additional production, we believe that our mandate of coordinating the NGPA and the NGA would best be accomplished through a policy of pricing parity among independent and pipeline producers.[16]

Generally, the Commission's Order No. 98 continued cost-of-service pricing only for pipeline production from wells drilled before January 1, 1973, on leases acquired before October 8, 1969. Even for that portion of pipeline production, there is no doubt that Congress intended to eliminate cost-of-service pricing and substitute uniform, congressionally-established incentive prices. As Congressman John D. Dingell, Floor Manager of the NGPA and Chairman of the Subcommittee on Energy and Power of the House Interstate and Foreign Commerce Committee, commented:

> The most important provisions of the bill are those which deal with wellhead pricing. These establish a schedule of price ceilings applicable to specifically defined categories of gas production. The result is the creation of a

[16] App. B-25.

> single, national market for natural gas and an end to the economic distortions which accompanied an outdated mode of regulation under the Natural Gas Act.[17]

The Fifth Circuit recognized that the NGPA supplanted the pre-existing system of regulation. It stated: "The Commission's duty is to administer the law Congress passed in light of the purposes for which it was passed. It is not an agency's prerogative to alter a statutory scheme even if its alteration is as good or better than the Congressional one." (App. A-9).

III. The Economic Impact Of Section 2(21)(B) Of The Natural Gas Policy Act Is Not Relevant To Its Interpretation

Petitioners allege that "massive windfall profits ... will accrue to a significant number of pipelines as a result of the opinion below". (PSCNY Pet. at 20). The court below properly declined to consider the economic impact of its interpretation of NGPA section 2(21)(B). The case before it was one of statutory interpretation. As the Fifth Circuit had previously observed in *Pennzoil Co. v. FERC*: "*Congress* carefully considered the economic

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[17]124 Cong. Rec. H13114 (daily ed. Oct. 14, 1978).

Petitioners place great emphasis on the fact that the court below did not "defer" to the expertise of the Commission in "interpreting" the term "first sale". But, as the court below pointed out, no deference was due. Congress defined the term "first sale" and, as a congressionally-defined term, that definition, not the Commission's, is binding on the court. *See* Conoco, Inc. v. FERC, 622 F.2d 796, 798 (5th Cir. 1980).

impact of the NGPA in designing that Act."[18] It is not for the courts to pass judgment on the policy decisions made by Congress. *Baker v. Carr*, 369 U.S. 186, 217 (1962).

The proper role for the court below, which it judiciously undertook, was to ascertain what Congress meant when it defined the term "first sale" and to determine whether the Commission's orders under review were inconsistent with that intent. Similarly, this Court should give no weight to Petitioners' assessment of economic impact in deciding whether to grant or deny the writ of certiorari.[19]

IV. The Decision Of The Fifth Circuit Does Not Conflict With The "Decision" Of The West Virginia Supreme Court

Petitioners State of Michigan (No. 81-2042) and Arizona Electric Power Cooperative, Inc. (No. 81-1958) suggest that this Court should grant a writ of certiorari to review the Fifth Circuit's decision because the decision conflicts with a decision of the West Virginia Supreme Court. The decision referred to by the Petitioners is

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[18]645 F.2d 360, 379 n. 37 (5th Cir. 1981) (emphasis added). In support of that proposition the court cites H.R. Rep. No. 496, pt. IV. 95th Cong., 1st Sess. 96-101, 110-21 (1977); Natural Resources and Commerce Division, Congressional Budget Office, The Natural Gas Compromise (Aug. 2, 1978), *reprinted in*, 124 Cong. Rec. H12126-27 (daily ed. Oct. 14, 1978); Energy Information Administration, U.S. Dep't of Energy, Analysis Memorandum No. AM/1A-7902, An Evaluation of Natural Gas Pricing Proposals (June 14, 1978).

[19]The economic impact data presented by the several petitioners is extra-record, unsupported, and speculative. While Consolidated does not want to engage in similar tactics, it is indisputable that pipeline production subject to cost-of-service pricing on the date of enactment of the NGPA was only a small, rapidly-diminishing portion of total domestic natural gas production. It follows, therefore, that the economic impact of the court's interpretation represents only a small fraction of the total economic impact of NGPA.

Pennzoil Co. v. Public Service Comm'n of W. Va., No. 80-175-G-42T, pending before this Court on Petition For A Writ of Certiorari in No. 81-1672. The decision of the West Virginia Supreme Court does not create a conflict with the opinion below.

That decision left intact a decision of the Public Service Commission of West Virginia refusing to permit Pennzoil Company to collect NGPA rates for its West Virginia natural gas production sold at retail in West Virginia. In its order denying Pennzoil's rate request, the Public Service Commission stated several independent grounds for its decision which were based on state law and not on the NGPA's "first sale" definition.[20]

The West Virginia Supreme Court did not state why it denied Pennzoil's petition for appeal. Because the basis of the court's decision is not apparent, it cannot be inferred that the court relied upon any definition of the term "first sale" that conflicts with that of the Fifth Circuit in the decision below. *Monrosa v. Carbon Black Export, Inc.*, 359 U.S. 180 (1959).

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[20]The order of the West Virginia Supreme Court is reproduced in the Appendix to the Petition For Certiorari To The Supreme Court of West Virginia filed by Pennzoil Company in No. 81-1672 App. B.

CONCLUSION

For these reasons, the petitions for a writ of certiorari should be denied.

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Opposition

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Nos. 81-1889, 81-1958, 81-2042, and 81-2119

Supreme Court, U.S.
FILED
AUG 5 1982
ALEXANDER L. STEVAS,
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, ARIZONA ELECTRIC POWER COOPERATIVE, INC., STATE OF MICHIGAN, AND FEDERAL ENERGY REGULATORY COMMISSION,

Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,

Respondents.

On Petitions For A Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

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BRIEF OF EL PASO NATURAL GAS COMPANY IN OPPOSITION

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QUESTION PRESENTED

Whether the Court of Appeals, in reviewing orders of the Federal Energy Regulatory Commission, properly construed the definition of "first sale" of natural gas set forth in Section 2(21) of the Natural Gas Policy Act of 1978 as applying to the intra-company transfer of natural gas produced by pipeline and local distribution companies and sold as part of their general system supplies.

TABLE OF CONTENTS

	Page
STATEMENT OF THE CASE	2
I. Introduction	2
II. Regulation Of Natural Gas Prior To The NGPA	4
III. The Natural Gas Policy Act Of 1978	7
IV. The Proceedings Below	8
REASONS FOR DENYING THE WRIT	10
SUMMARY OF ARGUMENT	10
ARGUMENT	11
I. The Lower Court Properly Held That The NGPA Accords Pipeline Production "First Sale" Treatment, Even When Commingled With Purchased Gas Supplies	11
II. The Lower Court's Decision Does Not Disrupt FERC Or State Regulation Of Pipelines And Distributors Nor Raise Other Public Interest Considerations Warranting Review	17
III. No Conflict Exists Between The Lower Court's Ruling In This Case And The Decision Of The West Virginia Supreme Court In *Pennzoil*	21
CONCLUSION	23

TABLE OF AUTHORITIES

CASES: Page

Colorado Interstate Gas Co. v. *FPC*, 324 U.S. 581 (1945) 5

Conoco, Inc. v. *FERC*, 622 F.2d 796 (5th Cir. 1980) .. 12

FPC v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944) .. 4

Just and Reasonable Rates for Sales of Natural Gas, 52 F.P.C. 1604 (1974), *aff'd sub nom.*, *Shell Oil Co.* v. *FPC*, 520 F.2d 1061 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976) 7

Mobil Oil Corp. v. *FERC*, 417 U.S. 283 (1974) 5

Pennzoil Co. v. *Public Service Commission of West Virginia*, Case No. 80-175-G-42T (S. Ct. of Appeals of W. Va., December 10, 1981), *petition for cert. filed*, Case No. 81-1672 21

Permian Basin Area Rate Cases, 390 U.S. 747 (1968). 5, 6

Phillips Petroleum Co. v. *Wisconsin*, 347 U.S. 672 (1954) 4, 5

Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738 (1969), *reh'g denied*, 42 F.P.C. 1089 (1969), *aff'd sub nom.*, *City of Chicago* v. *FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972). 6

Pipeline Production Area Rate Proceeding (Phase II), 47 F.P.C. 1523 (1972) 7

United Gas Improvement Co. v. *Continental Oil Co.*, 381 U.S. 392 (1965) 13

STATUTES:

Natural Gas Act, 15 U.S.C. § 717 ..... *passim*

Natural Gas Policy Act of 1978, Pub. L. No. 95-621, 92 Stat. 3350 (1979), 15 U.S.C. (Supp. IV 1980) §§ 3301, *et seq.* ..... *passim*

Section 2(20), 15 U.S.C. (Supp. IV) §§ 3301(20) 13

Section 2(21), 15 U.S.C. (Supp. IV), § 3301(21) 3, 8

Section 2(21)(A)(v), 15 U.S.C. (Supp. IV) § 3301(21)(A)(v) 16

Section 2(21)(B), 15 U.S.C. (Supp. IV) § 3301(21)(B) 8, 14

Section 101(b)(5), 15 U.S.C. (Supp. IV) § 3311(b)(5). 18

Table of Authorities Continued

Page

Section 102, 15 U.S.C. (Supp. IV) § 3312 18
Section 103, 15 U.S.C. (Supp. IV) § 3313 18
Section 104, 15 U.S.C. (Supp. IV) § 3314 ..... 18, 19
Section 107, 15 U.S.C. (Supp. IV) § 3317 18
Section 108, 15 U.S.C. (Supp. IV) § 3318 .... 18, 19, 20
Section 203(b)(1), 15 U.S.C. (Supp. IV) § 3343(b)(1) 14, 15
Section 203(b)(2), 15 U.S.C. (Supp. IV) § 3343(b)(2) 14, 15
Section 601(b)(1)(E), 15 U.S.C. (Supp. IV) § 3341(b)(1)(E) 15, 21
Section 602, 15 U.S.C. (Supp. IV) § 3432 21

REGULATIONS:

18 C.F.R. § 154.38(d)(4) (1981) 12

MISCELLANEOUS:

H.R. Rep. No. 95-1752, 95th Cong., 2nd Sess. 16

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

Nos. 81-1889, 81-1958, 81-2042, and 82-19

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, ARIZONA ELECTRIC POWER COOPERATIVE, INC., STATE OF MICHIGAN, AND FEDERAL ENERGY REGULATORY COMMISSION,

Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,

Respondents.

On Petitions For A Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

BRIEF OF EL PASO NATURAL GAS COMPANY IN OPPOSITION

EL PASO NATURAL GAS COMPANY (hereinafter "El Paso"),[1] an intervenor in the proceedings below, respectfully submits this brief in opposition to the peti-

[1] All of the issued and outstanding common stock of El Paso is owned by The El Paso Company. All of El Paso's subsidiaries are wholly owned, either directly or indirectly, by El Paso. El Paso's affiliates which are not wholly owned, either directly or indirectly, by The El Paso Company are Geo Nuclear Nobel Paso and Desert American Insurance Agency, Inc.—Virginia.

tions for a writ of certiorari[2] to review the opinion and judgment of the United States Court of Appeals for the Fifth Circuit in *Mid-Louisiana Gas Company, et al.* v. *Federal Energy Regulatory Commission*, Nos. 80-3804, *et al.*, issued December 23, 1981.

STATEMENT OF THE CASE

I. Introduction

This case concerns the application of the Natural Gas Policy Act of 1978, Pub. L. No. 95-621, 92 stat. 3350 (1979) (codified at 15 U.S.C. (Supp. IV 1980) §§ 3301, *et seq.*) (hereinafter "NGPA") to natural gas produced by interstate pipeline companies, intrastate pipeline companies and local distribution companies. Respondent El Paso is an interstate pipeline company.

Most of the nation's natural gas is produced by "independent producers," so called because such producers do not own pipeline transmission facilities (other than small diameter gathering pipelines located in the producing fields). A number of interstate pipeline companies including El Paso, as well as certain intrastate pipeline companies and local distribution companies, however, in addition to purchasing gas from independent producers or other suppliers, have found and produce their own natural gas reserves. (For ease of reference, such production, whether produced by a pipeline or distribution com-

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[2] This brief in opposition responds to the petitions for a writ of certiorari filed by the Public Service Commission of the State of New York (hereinafter "New York") in No. 81-1889, Arizona Electric Power Cooperative, Inc. (hereinafter "AEPCO") in No. 81-1958, the State of Michigan (hereinafter "Michigan") in No. 81-2042, and the Federal Energy Regulatory Commission (hereinafter "Commission" or "FERC") in No. 82-19. By Order dated June 8, 1982, the Clerk of the Court granted respondents until August 4, 1982, to file briefs in opposition to the foregoing petitions.

pany, generally will be referred to herein as "pipeline production" or "pipeline-produced gas".) Pipeline-produced gas is typically introduced into the transmission facilities owned by the pipeline company, where it is physically commingled with natural gas that has been purchased from independent producers, and these commingled supplies are then sold in an undifferentiated stream to the pipeline's customers.[3]

The pricing provisions of Title I of the NGPA, by their terms, apply solely to "first sales"[4] of natural gas, as that term is defined in Section 2(21) of the statute, 15 U.S.C. (Supp. IV) § 3301(21). In the administrative orders that are the subject of this case, the FERC concluded that pipeline production would be the subject of a "first sale" *only if* the sale involved gas volumes comprised "exclusively" of natural gas that had been produced from "wells, properties, or reservoirs" which were owned by a pipeline and was not sold as a part of its general system supplies. Since, in almost all cases, pipeline production is in fact commingled with gas that has been purchased from others, this approach effectively excluded from the coverage of Title I virtually all pipeline-produced gas.

On review, a unanimous panel of the United States Court of Appeals for the Fifth Circuit rejected the Commission's construction of the statutory "first sale" defini-

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[3] Many pipeline companies and distributors also own or are under common ownership with affiliated natural gas production companies. In recent years, such affiliated producers have been regulated on the same basis as independent producers and were so treated, for purposes of applying the NGPA, in the administrative orders that are the subject of this case. No party has contested this aspect of such orders.

[4] The term "first sale" is a term of art, having no history of usage in the pricing of natural gas under the Natural Gas Act.

tion. In a thorough and well-reasoned opinion, the court below held that the "language, purposes and history of the NGPA" all clearly revealed Congress' intent to accord "first sale" treatment to pipeline-produced gas.

II. Regulation Of Natural Gas Prior To The NGPA.

The petitioners in this case have relied extensively on their view of the state of pipeline production regulation prior to enactment of the NGPA. On analysis, however, it is apparent that the petitioners have essentially recast the history of that regulation to create the impression that pipeline production was treated on a fundamentally different basis from gas produced by independent producers. In fact, this purported difference is largely illusory.

In the Natural Gas Act of 1938 (hereinafter "NGA") 15 U.S.C. § 717, the Commission's predecessor, the Federal Power Commission (hereinafter "FPC"), was authorized to regulate the sale for resale and the transportation of natural gas in interstate commerce. Prior to this Court's decision in *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954), the FPC regulated sales by pipeline companies to their customers but, believing it lacked the power to do so, did not attempt to regulate sales by independent producers to pipelines. Within this pre-*Phillips* framework, the FPC was called upon quite early to determine how gas reserves and gas production that were owned by pipelines should be valued in rates.

In *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944), this Court approved a methodology which valued pipeline production by reference to the pipeline's prudent investment in the production aspects of its business. *Id.* at 606-617. Under this approach, pipeline rates would include amounts intended to permit the pipeline to recover the cost of operating its production properties plus a fair

return on the invested capital included in its rate base. (This approach later came to be called the cost-of-service method of valuation.) Shortly thereafter, in *Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945), the Court reaffirmed its approval of this method of valuing pipeline production, but noted: "We do not say that the Commission lacks the authority to depart from the rate-base method. We only hold that the Commission is not precluded from using it." *Id.* at 601.

As a result of this Court's holding in *Phillips*, *supra*, the FPC in 1954 was required, for the first time, to undertake the regulation of sales for resale by independent producers. Although the FPC initially attempted to set producer rates on the basis of each producer's own costs (*i.e.*, in the same fashion as it was then valuing pipeline production), it soon became apparent, in light of the great number of independent producers which the FPC regulated, that such an approach was administratively unworkable. *See Permian Basin Area Rate Cases*, 390 U.S. 747, 756 (1968). The FPC thus turned to an "area rate" methodology whereby maximum rates for independent producers were prescribed on the basis of average production costs in a specified geographical area. *See Permian*, *supra; see also Mobil Oil Corp.* v. *FPC*, 417 U.S. 283 (1974). Under this methodology, the FPC considered the same costs as those examined under a company-by-company approach, but set rates on the basis of the average costs experienced in a given area by the producing industry as a whole, rather than the costs of each individual producer. In 1976, the FPC applied essentially the same average cost approach to prescribe a single, nationwide rate for independent producer sales of gas from wells drilled after a specified date.

In 1964, while the first area rate proceeding was still pending before it, the FPC instituted a rulemaking to

determine whether it should also depart from the individual company cost-of-service methodology then being used to value pipeline production. In October 1969, shortly after its initial venture into area rate pricing was upheld in *Permian*, *supra*, the FPC did indeed conclude that cost-of-service pricing should be abandoned for pipeline production on leases acquired after the date of its decision. Finding that the contribution made by pipelines to total interstate gas production had been steadily declining over a number of years and that pipeline drilling efforts are exposed to the same costs as those of independent producers, the FPC held that pipeline production from leases acquired on or after October 8, 1969, should generally be priced on a parity with gas produced by independent producers. Under this rule, therefore, pipelines were required to value such production in their rates on an area (and, later, national) rate basis.[5] *See Pipeline Production Area Rate Proceeding (Phase I)*, 42 FPC 738, *reh'g denied*, 42 FPC 1089 (1969), *aff'd sub nom., City of Chicago* v. *FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972). This rule however, did permit pipelines to propose, upon a showing of special circumstances, a method other than area-rate pricing for their production.[6]

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[5] Although the FPC's departure from "cost-of-service" treatment might imply that the new pipeline production rates were not cost-based, such an implication would not be correct. In fact, area rates were themselves cost-based and constituted a form of cost-of-service price regulation. Thus, while El Paso will use the term "cost-of-service pricing" to refer to the Commission's practice of valuing pipeline production on the basis of each pipeline's own costs, the term could also be appropriately applied to area and national rate pricing.

[6] A proceeding to determine whether the Commission should abandon cost-of-service pricing with respect to leases acquired before October 8, 1969, was ultimately terminated by an order which

In 1974, the Commission broadened its parity pricing rule still further to include pipeline-produced gas from any well commenced on or after January 1, 1973, irrespective of the date on which the lease was acquired. *See Just and Reasonable Rates for Sales of Natural Gas*, 52 FPC 1604, 1656 (1974), *aff'd sub nom., Shell Oil Co.* v. *FPC*, 520 F.2d 1061 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976). Thus, although FPC regulation of older categories of pipeline production continued to be valued on a cost-of-service basis, all gas produced by pipelines on leases acquired on or after October 8, 1969, or from wells drilled on or after January 1, 1973, on other leases, has been priced on the same basis as gas sold by independent producers (unless an exception was granted based on a showing of special circumstances).

III. The Natural Gas Policy Act Of 1978

In the NGPA, the Congress fundamentally restructured federal regulation of natural gas producer pricing. During the years preceding enactment of the NGPA, buyers within the intrastate gas market were consistently able to outbid interstate buyers for new gas supplies. Moreover, the nation as a whole was annually consuming substantially more gas than was being discovered, with the result that gas reserves were declining dramatically and curtailments of interstate gas deliveries were commonplace. In the NGPA, the Congress undertook to ad-

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directed that the question be considered in individual pipeline company rate proceedings. *Pipeline Production Area Rate Proceeding (Phase II)*, 47 FPC 1523 (1972). Contrary to the Commission's assertion (Commission Pet. at 6-7), therefore, the Commission did not then or later decide that cost-of-service pricing for such production should necessarily be retained.

dress these problems principally by prescribing, in Title I, a series of maximum lawful ceiling prices for the "first sale" of various categories of natural gas. The "first sale" definition was so drawn that ceiling prices would apply regardless of whether the gas was being sold in the interstate or intrastate market. Moreover, Congress sought to stimulate new exploration and development by prescribing incentive ceiling prices for gas produced from newer wells, as well as gas in certain high-cost categories, in lieu of cost-based prices established by the Commission's area and national rate orders. The statute further provided that, on specified dates, all price controls over first sales of gas in several categories would be eliminated.

Prices established under Title I of the NGPA apply to all "first sales" of natural gas. Section 2(21) generally defines a "first sale" to be "any sale of any volume of natural gas" to an interstate pipeline, intrastate pipeline, local distribution company, or end-user, or any sale which precedes such sales. Under Section 2(21)(B), however, a sale *by* a pipeline or local distribution company (or one of their affiliates) would not be a "first sale" "unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof." 15 U.S.C. (Supp. IV) § 3301(21)(B). Section 2(21)(B) thus excludes from the first sale pricing rules resales of gas which was acquired by pipelines and distributors in first sales.

IV. The Proceedings Below

In Order No. 58,[7] issued November 17, 1979, the Commission determined that, under Section 2(21)(B), pipeline

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[7] 44 Fed. Reg. 66577 (1979). Order No. 58 is reproduced in Appendix B to New York's Petition for Certiorari, No. 81-1889. ("Pet. App.", as used hereinafter, refers to the Appendix to New York's Petition for Certiorari.)

or distributor production would be sold in a "first sale" only "to the extent such sale is comprised *exclusively* of production volumes of natural gas from identifiable wells, properties, or reservoirs which are owned by such pipeline or distributor." (Pet. App. B at 12; emphasis supplied.) In so holding, the Commission rejected the contention that a first sale should be deemed to occur at the point pipeline production is delivered into a pipeline's transmission system. The principal effect of the Commission's interpretation was to deny first sale treatment to all pipeline production except such incidental amounts as might be sold by a pipeline "off-system." The Commission thus left most pipeline production subject to regulation pursuant to the NGA. In contrast, Order No. 58 determined that sales by a production affiliate to a pipeline would be first sales under the NGPA.

Subsequently, in Order No. 98,[8] the Commission issued regulations under the NGA generally permitting pipeline production to be valued at the equivalent of NGPA ceiling prices, but provided that production from leases which had earlier been subject to cost-of-service treatment, either by regulation or because it was subject to an exception from area or national rate pricing, would continue to be valued on that basis. In Order No. 102,[9] issued October 3, 1980, the Commission denied rehearing of Order Nos. 58 and 98.

On appeal, the United States Court of Appeals for the Fifth Circuit vacated both Order Nos. 58 and 98. *Mid-Louisiana Gas Co. v. FERC*, 664 F.2d 530 (1981) (Pet. App. A). The lower court noted that the Commission's interpretation, by denying "first sale" treatment to virtually all pipeline production, was manifestly contrary to the Congress' intent. Relying on the language of Sec-

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[8] 45 Fed. Reg. 53091 (1980); Pet. App. B at 14-49.

[9] 45 Fed. Reg. 67083 (1980); Pet. App. B at 50-82.

tion 2(21), as well as other provisions of the statute and the legislative history, the court concluded that "Congress both intended to accord pipeline production first sale status and contemplated that the intracorporate transfer [from a pipeline's producing division to its transmission division] would be treated as a first sale." (Pet. App. A at 11). Following the denial of rehearing and rehearing *en banc* (Pet. App. C at 3-4), and issuance of the court's mandate (Pet. App. C at 1-2) on March 2, 1982, petitions for certiorari were filed with this Court.

REASONS FOR DENYING THE WRIT

SUMMARY OF ARGUMENT

The petitions in this case do not raise any novel or important questions of law. Rather the only issue presented is whether the lower court properly rejected an administrative interpretation of the NGPA first sale definition which gave essentially no effect to the statutory provision at issue. Because the court applied well-established rules of statutory construction, accorded the Commission's interpretation the proper amount of judicial deference, and correctly decided the question before it, review by this Court is unnecessary and inappropriate.

Moreover, the case presents no other grounds warranting review. Contrary to petitioners' claims, the lower court's decision does not create a "windfall" for pipelines by conferring excessive prices on older categories of gas supplies dedicated to their systems. Rather, to the extent that prices increase, it will be largely because the incentive price provisions applicable to newer gas production are working as Congress intended. While some price increases for older categories of pipeline production may occur, it is also possible that substantial quantities of this gas will in fact be priced below the levels prevailing at the time the NGPA was enacted.

ARGUMENT

I. The Lower Court Properly Held That The NGPA Accords Pipeline Production "First Sale" Treatment, Even When Commingled With Purchased Gas Supplies

In a thorough and careful opinion, the lower court held that the language, history and plain intent of the NGPA compelled the conclusion that pipeline production is subject to the "first sale" provisions of Title I of the statute. In so holding, a unanimous panel of that court properly rejected the Commission's view that, by defining "first sales" to *include* sales "attributable to" pipeline production, Congress paradoxically intended to *exclude* from this definition virtually all pipeline produced gas. As the court noted, such a construction "would effectively read . . . out of the NGPA" the very language at issue in this case. (Pet. App. A at 8). Indeed, the Commission's interpretation is directly contrary to the manifest purposes of the statute, since it would deny the carefully designed statutory incentives for new gas exploration, as well as the uniform wellhead pricing requirements, to a significant, if limited, component of the nation's natural gas production.[10]

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[10] In its decision, the Court of Appeals paid careful heed to the admonitions of this Court relating to the quantum of judicial deference owed to administrative agency interpretations of statutory terms. The lower court pointed out that the "first sale" concept is new to energy regulation, that the term does not bring into play the experience which the agency has gained in administering the NGA, nor does the definition draw on the agency's expertise in dealing with technical problems associated with energy regulation. Further, the Commission admitted that it had no input into the congressional development of the term "first sale." In light of these factors, the court concluded that it was not required to accept a Commission interpretation of the statute which was contrary to its clear meaning as revealed in the statutory language, purpose and history. (Pet. App. A at 15).

In reaching its interpretation, the court of appeals gave studied consideration to each of the arguments which the petitioners now seek to advance before this Court. The petitioners rely heavily on their contention that an intracorporate transfer of pipeline production cannot be a first sale because no "sale," in the traditional sense, has occured. Their argument, however, conveniently ignores the longstanding practice of the FERC and its predecessor, the FPC, of valuing most pipeline production initiated since October 1969 precisely as if it had been the subject of a sale at the wellhead.

Under regulations adopted by the FERC in 1969, and broadened in 1974, all pipeline production from leases acquired on or after October 8, 1969, or from wells drilled after 1972 on pre-October 8, 1969 leases (unless the subject of a special order providing for different treatment) has been priced in pipeline rates on exactly the same basis as gas purchased from independent producers. Further, the cost of such production was required to be included in each company's "purchased gas cost" rate adjustments in the same manner as the cost of gas purchased from others. *See* 18 C.F.R. § 154.38(d)(4), n.1 (1981). Rather than being a "novel regulatory doctrine" as the Commission claims (Commission Pet. at 14), the NGPA as interpreted by the lower court does no more than codify the Commission's own predominant treatment of pipeline production initiated since October 1969. *Cf. Conoco, Inc.* v. *FERC*, 622 F.2d 796, 798 (5th Cir. 1980) ("A statute or a definition contained within it may draw upon antecedent facts for its operation.") In these circumstances, therefore, the statute can hardly be said to "overturn 40 years of regulatory policy" as the Commission contends. (Commission Pet. at 20).

The lower court's holding, moreover, is fully consistent with a literal application of the "first sale" definition of Section 2(21). The statutory language manifests a clear intent to accord the term "first sale" the widest possible application. The term "sale" itself is elsewhere defined to embrace "*any* sale, exchange *or other transfer for value.*" 15 U.S.C. (Supp. IV) § 3301(20) (emphasis supplied). Thus, in construing the "first sale" definition to include intracorporate transfers of pipeline production, the lower court properly declined to find a congressional intent to incorporate in the Act narrow common or state-law rules governing "sales." *Cf. United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392, 400 (1965) (a regulatory statute "would be hamstrung if it were tied down to technical concepts of local law.")

More importantly, the court gave full and proper effect to the literal and unqualified scope of the first sale definition—a definition expressly embracing all pipeline sales that are "*attributable to*" gas which that pipeline has produced. Contrary to petitioners' claims, this language is barren of any hint that Congress was concerned to limit first sale treatment to isolated and incidental "off-system" pipeline sales. Thus, the court below correctly concluded that, by employing the phrase "attributable to," Congress intended to confer first sale treatment on a pipeline's acquisition of its own production in the same manner that the first sale definition applies to independent producer sales and, as the Commission acknowledged, to transfers between affiliates.

Whatever ambiguity arguably resides in the "first sale" definition is wholly dispelled in any event by other provisions of the statute or its legislative history. While, as certain petitioners have observed, these other indicia of legislative intent might not be ultimately controlling, the fact remains that *nowhere* in the legislative record did the

Congress address pipeline production in terms that do other than confirm its first sale status.[11] Thus, the incremental pricing provisions of Title II are explicitly premised on the assumption that intracorporate transfers of pipeline production are first sales. For purposes of the incremental pricing program, a "first sale acquisition cost" is generally defined as the "price paid" in a first sale, 15 U.S.C. (Supp. IV) § 3343(b)(1); while for pipeline and affiliate production, Section 203(b)(2) provides as follows:

> (2) INTERSTATE PIPELINE PRODUCTION—For purposes of this section, in the case of any natural gas produced by any interstate pipeline or any affiliate of such pipeline, the first sale acquisition cost of such natural gas shall be determined in accordance with rules prescribed by the Commission.

15 U.S.C. (Supp. IV) § 3343(b)(2). As the court of appeals aptly noted, by this language "Congress must have contemplated that any gas produced by a pipeline would be subject to a first sale." (Pet. App. A at 11).

Both the Commission and New York contend that Section 203(b)(2) would be unnecessary if intracorporate transfers of pipeline production are "first sales," since the "price paid" for pipeline production would simply be the

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[11] The Commission quotes a House of Representatives report which states that a "first sale" is intended to mean an "arms-length transaction." Commission Pet. at 16-17. This report, however, addressed the legislation *before* it was revised to include an express "first sale" definition and thus did not consider the provision in Section 2(21)(B) dealing with the transfer of pipeline production. That the language from the House report has no application to this case is clear from the fact that the NGPA *as enacted* applies, by all parties' admission, to sales between affiliates which, by definition, are not at arms'-length.

applicable NGPA ceiling price. (Commission Pet. at 23; New York Pet. at 16.) This assertion is obviously incorrect. Not only does Section 203(b)(2) recognize that intracorporate transfers technically do not involve a "price paid" and, for that reason, do not come clearly within the general rule of Section 203(b)(1), first sales of pipeline production are not necessarily entitled to Title I ceiling prices as these parties assume. Although the effect of the Fifth Circuit's decision is that first sale prices for interstate pipelines will be determined in accordance with the provisions of the NGPA, the statute does not guaranteee that maximum ceiling prices will apply. Rather, any amounts paid in first sales between affiliates are subject to the "comparable sales" restriction of Section 601(b)(1)(E), 15 U.S.C. (Supp. IV) § 3431(b)(1)(E).[12] Section 203(b)(2), therefore, not only makes clear that pipeline production results in a *first sale* acquisition cost, but it also permits the Commission to assure that the cost of such production will be determined in accordance with any regulatory restrictions applicable to pricing of such production.

The argument of these petitioners proves too much in any event. Section 203(b)(2) by its terms applies not only to pipeline production but also to any purchase from an affiliate of a pipeline. Since both the Commission and New York agree that affiliate sales are clearly first sales, the logic of their claim would necessarily imply that Section

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[12] Section 601(b)(1)(E) provides in pertinent part:

AFFILIATED ENTITIES LIMITATION.—. . . in the case of any first sale between any interstate pipeline and any affiliate of such pipeline, any amount paid in any first sale shall be deemed to be just and reasonable if . . . such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.

203(b)(2) has no purpose whatsoever. In fact, this provision demonstrates that, for NGPA purposes, intracorporate transfers of pipeline production stand on precisely the same footing as any other affiliate transfer.

The Conference Report respecting the NGPA also makes clear Congress' understanding that intracorporate transfers of pipeline production are first sales. *See* H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 116, reprinted in 1978 U.S. Code Cong. & Ad. News 9033. Indeed, the conferees' statement that the Commission "may also establish rules applicable to intracorporate transactions under the first sale definition" directly contradicts petitioners' contention that intracorporate transactions can never be first sales.

The Commission's view (Commission Pet. at 19) that this statement merely acknowledges its discretionary power to treat intracorporate transfers of pipeline production as first sales is similarly flawed. Under Section 2(21)(A)(v), which is the only statutory basis for expanding the "first sale" definition, the Commission is authorized to define "any sale" as a "first sale" when necessary "to prevent circumvention of any maximum lawful price established" under Title I. If intracorporate transfers of interstate pipeline production were not by definition first sales, however, this provision clearly would not enable the Commission to define them as such since first sale treatment of pipeline production could not be justified on the ground of preventing circumvention of the Act.[13] Instead, the conferees' statement can be reconciled with the statutory scheme only if the first sale

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[13] Under the Commission's interpretation, interstate pipeline production would remain fully subject to the provisions of the Natural Gas Act, and, therefore, circumvention of the statute would be impossible.

definition is understood as conferring first sale status on intracorporate transfers of pipeline production.

In sum, the court of appeals' decision is fully consistent with the language, history and purpose of the NGPA, and, accordingly, need not be reviewed by this Court.

II. The Lower Court's Decision Does Not Disrupt FERC Or State Regulation Of Pipelines And Distributors Nor Raise Other Public Interest Considerations Warranting Review

The petitions for certiorari claim that the effect of the court of appeals' decision in this case is to "repeal by implication" longstanding federal regulation of pipeline production, permit unwarranted price increases by pipelines and distributors and otherwise adversely impinge on the public interest. These hyperbolic claims are uniformly unfounded and rest on serious misconceptions regarding the effect of the NGPA on pipeline production pricing.

The petitioners claim that Congress could not have intended to repeal, by implication, the FERC's authority under the NGA to regulate pipeline production on a "cost-of-service" basis. This argument not only assumes the very result at issue in this case, but it completely ignores the fact that under the NGA *all* rates established by the FERC for natural gas production, whether determined on an individual company or area-wide basis, were cost-based, and that a principal purpose of the NGPA was to replace such cost-based rate regulation of "new" gas with a system of incentive prices.[14] Since the Commission itself determined as early as October 1969 that the intracorporate transfer of pipeline production initiated after that date should generally be subject to the same

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[14] *See* Mid-Louisiana Gas Co. v. FERC, Pet. App. A at 9.

pricing rules as those applicable to independent producers, the court's interpretation works no change at all in the pricing rules applicable to substantial quantities of pipeline production.

While it is true that prior to the NGPA the Commission retained cost-of-service pricing for production from older pipeline wells, and prescribed such treatment for certain newer production under the "special circumstances" provisions of its pipeline production regulations, the effect of applying NGPA determined prices to this production does not lead to the "windfall" petitioners portray. In fact, to the extent consumer prices for pipeline production do increase, it will be largely because the NGPA is working as Congress intended.

Under Section 104 of the statute, 15 U.S.C. (Supp. IV) § 3314, ceiling prices for older production are based on the "just and reasonable" rates for such gas in effect prior to enactment of the NGPA.[15] Thus, the Act was specifically crafted to preserve existing cost-based ceiling prices for most flowing gas and to continue such controls, without provision for deregulation, until depletion of the wells. While it has not yet been determined how Section 104 will be applied to pipeline production, it is possible, as the FERC suggested in its brief to the Fifth Circuit,[16] that prices under Section 104 will be established for each

[15] Section 104 applies to all "gas committed or dedicated to interstate commerce on the day before the date of enactment of . . . [the NGPA] and for which a just and reasonable rate under the Natural Gas Act was in effect on such date. . . .," unless, by virtue of Section 101(b)(5), 15 U.S.C. (Supp. IV) § 3311(b)(5), the gas qualifies for an incentive price under Sections 102, 103, 107 or 108. The incentive price provisions of these latter sections apply, with the exception of Section 108 (*see* n.17, *infra*), only to relatively recent wells.

[16] "Brief for Respondent Federal Energy Regulatory Commission," No. 80-3804 (dated February 20, 1981) at 33.

pipeline on the basis of the production costs included in that company's rates at the time the NGPA was enacted. In such an event, little if any price increase would result. If, on the other hand, pipeline production must be priced at the rates prescribed under the Commission's area and national rate orders, then, while prices for some gas that is subject to Section 104 will probably increase, substantial quantities of such production may in fact experience a price decrease. In El Paso's case, for example, when area and national rates were applied to El Paso's wells subject to Section 104, a significant price reduction occurred.[17] Similarly, the 82 cent unit cost of Columbia Gas Transmission Company's production cited by New York (New York Pet. at 19), is substantially higher than FERC area rates for most older vintages of gas. The claims that the older categories of pipeline production will enjoy a windfall at the expense of consumers, therefore, are unfounded.

Under the lower court's construction of the statute, some existing or future pipeline cost-of-service production will obviously be eligible for one or another of the incentive prices established by the NGPA. This circumstance, however, does not justify the inference that Congress intended to exclude pipeline producers from the incentive pricing program applicable to all other producers. For the most part, NGPA incentive prices apply to natural gas produced from newer wells.[18] It is precisely

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[17] El Paso reflected such independent producer area and national rates for its Section 104 production in a rate change filed with the Commission on March 1, 1982 which was designed, in part, to reflect the impact of the Fifth Circuit's *Mid-Louisiana* decision.

[18] The principal exception to this rule is the incentive price established under Section 108, 15 U.S.C. (Supp. IV) § 3318, for "stripper well" production. "Stripper wells" are generally defined as wells having an average daily production of less than 60 Mcf (thousand

this category of production, of course, that the NGPA sought to encourage through provision of incentive prices. Although petitioners' desire to avoid price increases is understandable, the fact that such price increases occur does not, as petitioners contend, provide any basis for review by this Court. Such price increases clearly flow from the statute itself, and not from the lower court's decision in this case.

Many of the estimates made by *amici* concerning the effect of the NGPA on pipeline production prices are greatly inflated in any event, and are advanced without any support in the record or in fact. The Commission's own estimate is $100 million or more annually "for the next several years" (Commission Pet. at 15, n.11). While this amount is not insignificant, even it must be viewed in the context of producer price increases generally. When viewed against that backdrop, it is apparent that pricing pipeline production at NGPA rates may have only a marginal effect on consumer prices.

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cubic feet). By definition, therefore, stripper well gas is a relatively limited category of production. Some stripper well production will obviously occur on old leases and, therefore, Section 108 operates to increase the otherwise applicable Section 104 price. However, in El Paso's case at least, the overall increase in revenues available under Section 108 for its older production is far less than the revenue *decrease* El Paso incurs by applying area and national rates to the remainder of its Section 104 production. In any event, Section 108 represents the Congress' judgment that production from stripper wells, even if otherwise subject to a just and reasonable rate under Section 104, should be encouraged through the extension of economic incentives. Petitioners have not suggested any plausible reason why this incentive should apply to older vintages of gas produced by independent producers but not to pipeline production.

Petitioners' other claims regarding the allegedly disruptive effects of the lower court's decision are similarly without substance. First, the absence of contracts covering pipeline production does not, as petitioners claim, subject consumers to artificially inflated price increases. Section 601(b)(1)(E) of the NGPA, 15 U.S.C. (Supp. IV) § 3431(b)(1)(E), expressly restricts all "first sales" involving affiliates to prices not exceeding amounts paid in "comparable first sales between persons not affiliated with" the pipeline producer. This provision effectively assures consumers that they will pay for no more pipeline production than an amount that has been established at arms'-length.

Second, applying the NGPA to intrastate pipeline and distributor sales will not encroach on state regulation of such production. Under Section 602, 15 U.S.C. (Supp. IV) § 3432, the states are expressly authorized to prescribe first sale prices less than the maximum lawful ceiling prices otherwise lawful under Title I. Thus, to the extent purely local gas supplies are involved, the states retain all of their traditional powers to regulate gas prices.

III. No Conflict Exists Between The Lower Court's Ruling In This Case And The Decision Of The West Virginia Supreme Court In *Pennzoil*

Arizona Electric Power Cooperative, Inc. and the State of Michigan have claimed that the Fifth Circuit's decision in this case conflicts with the decision of the West Virginia Supreme Court in *Pennzoil Co.* v. *Public Service Commission of West Virginia*, Case No. 80-175-G-42T (S. Ct. of Appeals of W. Va., December 10, 1981), *petition for cert. filed*, Case No. 81-1672. The West Virginia court, however, was completely silent regarding the bases for its decision and, as pointed out by the Public Service

Commission of West Virginia itself,[19] the State court's opinion could have rested on a number of grounds having no relationship to the issue involved in this case. It is also notable that the FERC does not allege any conflict between these two decisions.[20] The make-weight argument of these petitioners should accordingly be rejected.

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[19] *See* "Response of The Public Service Commission of West Virginia to the Motion of Arizona Ele ' ic Power Cooperative, Inc. for Contemporaneous Consideration and Disposition of Pending Cases," filed in No. 81-1958.

[20] See also "Memorandum for the United States and the Federal Energy Regulatory Commission as Amicus Curiae," filed in No. 81-1672.

CONCLUSION

For the foregoing reasons, the petitions for certiorari filed in this case present no question warranting review of the decision of the lower court and, accordingly, should be denied.

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Opposition

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Nos. 81-1889, 81-1958, 81-2042 and 82-19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioner,
v.
MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
Petitioner,
v.
MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

STATE OF MICHIGAN,
Petitioner,
v.
MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

FEDERAL ENERGY REGULATORY COMMISSION,
Petitioner,
v.
MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Petitions for a Writ of Certiorari To The United States Court of Appeals For the Fifth Circuit

BRIEF IN OPPOSITION OF RESPONDENTS KANSAS-NEBRASKA NATURAL GAS COMPANY, INC. AND MICHIGAN WISCONSIN PIPE LINE COMPANY

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August 4, 1982

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QUESTION PRESENTED

It is undeniable and admitted that by passage of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3301, *et seq.*, (NGPA), the Congress made drastic, far reaching charges in the regulation of the natural gas industry, including elimination of Federal Energy Regulatory Commission (FERC) power and responsibility to regulate the price which *producers* of natural gas may receive for gas, by substituting *Congressionally* set or prescribed prices (and for both *intrastate* and interstate gas), and by deregulating certain categories of gas. In that context, the question is whether the United States Court of Appeals for the Fifth Circuit was correct in its interpretation of the NGPA, in the decision below, that Congress did *not* carve out an implausible exception, so as to allow continued price FERC regulation over *only* that relatively small volume of gas which is *produced* by natural gas *pipeline* companies. The Court of Appeals instead held that the clear language and purpose of the NGPA shows that Congress treated *all* producers, including pipeline producers, alike, without discrimination. The Court held invalid, the attempt by the Federal Energy Regulatory Commission to interpret a definition in the NGPA so as to allow the Commission to choose *which* gas produced by pipelines will be allowed to receive the Congressionally set prices.

These proceedings do *not* involve questions concerning the regulation of the overall functions of pipeline companies: the transportation of gas and the resale prices of gas sold. Those functions will remain subject to FERC regulation, if the decision below stands.

LISTING OF AFFILIATES PURSUANT TO RULE 28.1

Listed below, pursuant to Rule 28.1 of the Rules of the Supreme Court of the United States, are the affiliates of Respondents Kansas-Nebraska Natural Gas Company, Inc. and Michigan Wisconsin Pipe Line Company:

MICHIGAN WISCONSIN PIPE LINE COMPANY

American Natural Alaskan Company
American Natural Arctic Company
American Natural Offshore Company
American Natural Resources Company
American Natural Service Company
ANG Coal Gasification Company
ANR Coal Company
ANR Freight System, Inc.
ANR Gasification Properties Company
ANR Media Company
ANR Storage Company
ANR Western Coal Development Company
ANR Western Storage Company
Associated Central Terminal Company
Associated Trucklines, Inc.
Brooks Run Coal Company
Enterprise Coal Company
Garrett Forwarding Company
Garrett Freightlines, Inc.
Garrett Terminal Corporation
Graves Truck Line, Inc.
Great Lakes Gas Transmission Company
The Luper Transportation Company
New Life Transport Parts Center, Inc.
Road Equipment Financing, Inc.
Road Equipment, Inc.
VICC Land Company
VICCO Coal Company
VICCO International Sales Corporation
VICCO Leasing Company
Virginia Iron, Coal and Coke Company

KANSAS-NEBRASKA NATURAL GAS COMPANY, INC.

Cap-Con International, Inc.
Excelsior Oil Corporation
Kan-Col Company of Kansas
Midlands Gas Corporation
Midlands Transportation Co.
North Central Energy Company
Northern Gas Company
Northern Mountain Gas Co.
Northern Utilities, Inc.
Slurco, Inc.
Western Alfalfa Corporation
Western Alfalfa Transportation Systems, Inc.
Western Gas Corporation
Wyoming Fuel Company

WILLIAM W. BRACKETT
For the above named Petitioners

August 4, 1982

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
LISTING OF AFFILIATES PURSUANT TO RULE 28.1	ii
TABLE OF CONTENTS	iv
TABLE OF AUTHORITIES	v
COUNTER STATEMENT OF THE CASE	2
1. The Far Reaching Changes Made By The NGPA	3
2. The Unsupported Exception Which The FERC Claims	5
3. The Specific Issue: The Definition Of "First Sale"	7
4. The Opinion Below	10
SUMMARY OF ARGUMENT	11
REASONS THE PETITIONS SHOULD NOT BE GRANTED	12
I. THE OPINION BELOW IS NOT OF BROAD APPLICABILITY OR IMPORTANCE	14
II. THE OPINION OF THE COURT BELOW IS CORRECT	17
A. The Statutory Interpretation and Result Reached By The Court Below is Correct And Reasonable	17
B. The Decision Below Creates No Regulatory Problems For The FERC Or State Regulation	23
III. THE BASIS FOR DECISION OF THE ALLEGEDLY CONFLICTING DECISION CANNOT BE DETERMINED SO THAT NO CONFLICT CAN BE FOUND	27
CONCLUSION	30

TABLE OF AUTHORITIES

CASES Page

Amoco Production Co., et al. v. *DOE, et al.*, U.S. District Court for the District of Delaware, Dkt. Nos. Civil 78-463, April 9, 1981 (Fed. Energy Guidelines, p. 28,460) 26
Community-Service Broadcast of Mid-America, Inc. v. *FCC*, 593 F.2d 1102 (D.C. Cir. 1978) 23
Curren v. *Wallace*, 306 U.S. 1 (1938) 22
Davies Warehouse Co. v. *Bowles*, 321 U.S. 144 (1974) 22
Espinoza v. *Farah Mfg. Co.*, 414 U.S. 86 (1973) 22
Fed. Mar. Comm'n v. *Seatrain Lines, Inc.*, 411 U.S. 726 (1973) 22
FTC v. *Colgate-Palmolive Co.*, 380 U.S. 374 (1975) 21
Herweg v. *Ray*, 455 U.S. —— (1982), 102 S.Ct. 1059 21
Int. Bhd. of Teamsters, etc. v. *Daniel*, 439 U.S. 551 (1979) 22
Manhattan General Equipment Co. v. *Comm'r of Internal Revenue*, 297 U.S. 129 (1936) 22
Mid-Louisiana Gas Co., et al. v. *FERC*, 664 F.2d 530 (5th Cir. 1981) 2
Morton v. *Ruiz*, 415 U.S. 199 (1974) 22
Neuberger v. *Comm'r*, 311 U.S. 83 (1940) 22
NLRB v. *Brown*, 380 U.S. 278 (1965) 21, 22
Pennzoil Company v. *Pub. Serv. Comm'n of West Virginia*, No. 80-175-G-42T (Dec. 10, 1981) 27, 29
Phillips Petroleum Co. v. *Wisconsin*, 347 U.S. 672 (1954) 3
Schneider v. *Rusk*, 377 U.S. 163 (1964) 22
SEC v. *Sloan*, 436 U.S. 103 (1978) 21
Shea v. *Vialpando*, 416 U.S. 251 (1974) 22
United States Dept. of Agriculture v. *Moreno*, 413 U.S. 528 (1973) 23
Usery v. *First National Bank of Arizona*, 586 F.2d 107 (9th Cir. 1978) 22
Volkswagenwerk Aktiege v. *Fed. Mar. Comm'n*, 390 U.S. 261 (1968) 22

TABLE OF AUTHORITIES—Continued

STATUTES Page

Administrative Procedure Act, 5 U.S.C. § 500, *et seq.*
5 U.S.C. § 706(A) 22
5 U.S.C. § 706(B) 22
5 U.S.C. § 706(C) 22
Natural Gas Act, 15 U.S.C. §§ 717, *et seq.* ..... *passim*
Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301, *et seq.* ..... *passim*
§ 2(21) (15 U.S.C. § 3301(21)) ..... *passim*
§ 101 (15 U.S.C. § 3311) 4
§ 102 (15 U.S.C. § 3312) 4
§ 103 (15 U.S.C. § 3313) 4
§ 104 (15 U.S.C. § 3314) 4
§ 105 (15 U.S.C. § 3315) 4
§ 106 (15 U.S.C. § 3316) 4
§ 107 (15 U.S.C. § 3317) 4
§ 108 (15 U.S.C. § 3318) 4
§ 109 (15 U.S.C. § 3319) 4
§ 121 (15 U.S.C. § 3331) 4
§ 122 (15 U.S.C. § 3332) 4
§ 201 (15 U.S.C. § 3341) 5
§ 202 (15 U.S.C. § 3342) 5
§ 203 (15 U.S.C. § 3343) 5
§ 204 (15 U.S.C. § 3344) 5
§ 205 (15 U.S.C. § 3345) 5
§ 206 (15 U.S.C. § 3346) 5
§ 207 (15 U.S.C. § 3347) 5
§ 208 (15 U.S.C. § 3348) 5
§ 311 (15 U.S.C. § 3371) 5
§ 401 (15 U.S.C. § 3391) 5
§ 402 (15 U.S.C. § 3392) 5
§ 403 (15 U.S.C. § 3393) 5
§ 404 (15 U.S.C. § 3394) 5
§ 501 (15 U.S.C. § 3411(b)) 22
§ 601 (15 U.S.C. § 3431) 4, 5, 25
§ 602 (15 U.S.C. § 3432) 28

TABLE OF AUTHORITIES—Continued

OPINIONS AND ORDERS OF THE FERC Page

Order No. 58, Final Rule Covering the Maximum Lawful Price for Pipeline Distributor and Affiliate Production, Docket No. RM80-7 (November 14, 1979) ..... *passim*

Order No. 98, Final Rule Governing Pricing of Pipeline Production Under the Natural Gas Act, Docket No. RM80-6 (August 4, 1980) ..... *passim*

Order No. 102, Order Denying Rehearing of Order No. 58 and Order No. 98 and Clarifying Order No. 98, Docket Nos. RM80-6 and RM80-7 (October 3, 1980) 23

N'tl Fuel Gas Supply Corp., FPC Docket No. RP76-96, 18 FPS 5-829 (1979) 24

REGULATIONS OF THE FERC

18 C.F.R. § 270.203 22

18 C.F.R. § 270.203(c) 6

IN THE

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OCTOBER TERM, 1981

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On Petitions for a Writ of Certiorari To The United States Court of Appeals For the Fifth Circuit

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BRIEF IN OPPOSITION OF RESPONDENTS KANSAS-NEBRASKA NATURAL GAS COMPANY, INC. AND MICHIGAN WISCONSIN PIPE LINE COMPANY

COUNTER STATEMENT OF THE CASE

This case involves the interpretation of a definition in a statute: the definition of the term "first sale" in Section 2(21) of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. § 3301(21).

The United States Court of Appeals for the Fifth Circuit, in the opinion below (664 F.2d 530), carefully examined that definition and determined that if it were interpreted in the manner advocated by the Federal Energy Regulatory Commission (FERC), the plain meaning of the NGPA would be violated, and the result created would be in conflict with the clear intent of Congress, and otherwise legally insupportable.

This proceeding does *not* involve the authority of the FERC to regulate the prices which pipeline companies may charge for the gas they sell and transport under the Natural Gas Act, 15 U.S.C. § 717, *et seq.* (NGA): that authority is not in question. Instead, the issue here involves one of the costs which the FERC must allow in its price regulation of pipelines subject to its jurisdiction: the cost of the gas itself. (Other costs, *not* involved here, include the costs of processing, gathering, transporting, and selling the gas). No one denies the fact that in the NGPA, the Congress established the prices which may be charged by producers of natural gas, thereby eliminating pre-existing FERC authority, and required that such prices must be allowed by the FERC as the cost for the gas component of the pipeline costs which are used in fixing pipeline sales rates. The issue here is the claim

of the FERC that the Congress, *sub silentio*, carved out an exception to that action, but for *only* the relatively small quantity of gas *produced* (rather than purchased) by the pipelines themselves, and thus allowed the FERC to give that gas different price treatment than the Congress has required for all other gas. The Court below properly rejected that claim.

1. The Far Reaching Changes Made By The NGPA

The NGPA was one of a number of statutes enacted in 1978 in an attempt to deal with the growing energy shortage in the United States. The basic purpose of the NGPA was to establish a uniform national natural gas pricing policy, so as to assist and stimulate the production of natural gas by legislative mandate of increased allowable prices to all producers of interstate and intrastate natural gas.

The background of these proceedings is that prior to the passage of the NGPA, the pricing of natural gas which was sold by producers of gas, whether independent producers or pipeline producers, in *interstate* commerce, was determined and controlled by the FERC or its predecessor, the Federal Power Commission (FPC).[1] That same situation had existed for well over twenty years: *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954) held that independent producer pricing of interstate gas was subject to the NGA, and the FERC began to regulate all producers on a cost of service basis. The pricing of *intrastate* gas, however, was not subject to the Natural Gas Act or other federal pricing regulation.

The NGPA totally changed the above pattern.

First, the price control, and decontrol, provisions of the NGPA are applicable to intrastate, as well as interstate, gas, thus bringing intrastate gas under federal regulation provisions for the first time. This drastically changed many decades of past practice and law.

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[1] Both the FERC and the FPC are referred to herein as "FERC".

Second, the NGPA wholly changed the basic pattern of price controls over natural gas. Provision was made for the total elimination of governmental price controls over certain categories of natural gas.[2] As to those categories of gas which remain subject to governmental price controls, temporarily or permanently, the prices are no longer fixed by the FERC, but are instead fixed by the terms of the NGPA:[3] Congressionally established "maximum lawful prices" have replaced FERC discretion.[4] The prices previously fixed by the FERC for gas purchased and produced were used by the FERC as the "gas cost component" of the overall "cost of service" which the FERC computed—and still computes—in order to fix the rates which the pipelines may charge for their sales of gas. The NGPA has mandated the continuation of that practice, but using NGPA set prices, not FERC fixed producer prices. The FERC continues to regulate pipeline rates, so there is no lapse of consumer protection. The NGPA requires that the prices fixed *by Congress* in the NGPA be the "gas cost component" of the FERC computed "cost of service", since Congressionally set prices for the "gas cost component" have replaced FERC fixed prices.[5] This case has been created by the persistent, albeit selective, FERC resistance to that statutory requirement.

The NGPA also instituted other far reaching changes for the natural gas industry and its regulation, including such matters as mandatory "incremental pricing",[6] ad-

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[2] *See* NGPA, Section 121 (15 U.S.C. § 3331).

[3] *See* NGPA, Sections 101 through 109 (15 U.S.C. §§ 3311 through 3319).

[4] Further, the discretionary power to reinstitute price controls over certain categories of gas produced which will, under the NGPA, become decontrolled, was given to the President and Congress, not the FERC. See NGPA, Section 122 (15 U.S.C. § 3332).

[5] *See* NGPA, Section 601(c) (15 U.S.C. § 3431(c)).

[6] *See* NGPA, Title II, Sections 201 through 208 (15 U.S.C. §§ 3341 through 3348).

vance statutory general authorization of approval of certain transactions between interstate and intrastate gas companies,[7] statutory establishment of certain natural gas service curtailment policies,[8] and statutory exclusion of certain transactions from Natural Gas Act jurisdiction.[9]

It is in the context of the above described dramatic, far reaching changes in natural gas regulation that the narrow question presented herein arises.

2. The Unsupported Exception Which The FERC Claims

This proceeding involves the pricing of only natural gas *produced* by interstate natural gas pipeline companies themselves, for sale to their customers.[10] Such gas constitutes a quite small portion of the total quantity of gas transported and sold by the pipelines: the great bulk of their gas supply is purchased from "independent" (non-affiliated) producing companies, and from separate producing companies which are affiliated with the pipeline company ("independent producers" and "affiliate producers", respectively).

The pricing provisions of the NGPA do not refer to prices for gas produced by producing companies, or prices for gas produced by pipeline companies: no distinctions are made which relate to the identity of the *producer*. Instead, the pricing provisions simply fix a "maximum lawful price" [11] for each category of *gas*, without mention of the identity of the producer.[12]

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[7] *See* NGPA, Section 311 (15 U.S.C. § 3371).

[8] *See* NGPA, Sections 401 through 404 (15 U.S.C. §§ 3391 through 3394).

[9] *See* NGPA, Section 601(a) (15 U.S.C. § 3431(a)).

[10] The principles established by the decision below would affect gas produced by intrastate pipelines and distributors, as well as interstate pipelines, but reference is made herein to the latter because Petitioners below are interstate pipelines.

[11] Which is a stated price and a method for adjusting it, or an adoption of a prior fixed price, by reference, plus a method for adjustment. *See* note 3, *supra*.

[12] *See* note 3, *supra*.

The FERC, however, has alleged that it needed to issue a specialized regulation relative only to "maximum lawful prices" for gas produced by interstate *pipelines*. Such regulation, which is the subject of these proceedings, was issued by FERC Order No. 58, Final Rule Covering the Maximum Lawful Price for Pipeline Distributor and Affiliate Production, Docket No. RM80-7 (November 14, 1979) (App. B-1). In that order, the FERC stated circumstances under which gas produced and sold by interstate pipelines, *under the FERC view of the NGPA*, would be subject to prices fixed by the *FERC*, and *not* to NGPA pricing provisions, despite the Congressional removal of such previous FERC authority over *all other* gas. The regulation, therefore, is a claim by the FERC that it has the authority, despite the general removal of FERC pricing authority by the NGPA, to hold pipeline produced gas to prices other than those prescribed in the NGPA. Further, the FERC has claimed the power to pick and choose which pipeline produced gas would receive NGPA prices, and which would not. However, inconsistently, but correctly, Order No. 58 interpreted the *NGPA pricing provisions* to apply to gas produced and sold by producing companies which are *affiliates* of interstate pipelines, just as it does to other producers.[13]

It is thus apparent that the FERC, in Order No. 58:

a. Drew a distinction between gas produced by producers owned by or otherwise affiliated with a pipeline, and gas produced by the pipeline itself, even though no such distinction appears in the NGPA;

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[13] The portion of the regulation promulgated which relates to such "affiliate producers", Section 270.203 (c), 18 C.F.R. § 270.203(c), states that the FERC has authority to "not treat" such a sale as subject to the NGPA, "on application", and also may disqualify some of such sales (which are described so vaguely as to be unclear). Such reservations of alleged authority and possible exclusions have not been applied by the FERC and are not involved herein.

b. Created groupings within the volume of gas produced by pipelines, even though no such distinctions appear in the NGPA.

c. Claimed that a statutory provision was inserted to make only a miniscule share of pipeline produced gas subject to the NGPA pricing provisions.

d. As a result, held that certain thereby created "groupings" of gas produced by pipelines, which includes almost all of such gas, are still subject to *FERC* price controls, and not NGPA pricing provisions, even though the NGPA does not so state or indicate.

3. The Specific Issue: The Definition Of "First Sale"

The mechanism which the FERC has used, to attempt to support the above unsupported distinctions and results, is its definition of the term "first sale" in Section 2(21) of the NGPA. Since each pricing section of the NGPA states that the prices specified in that section "shall apply to the first sale of" the natural gas categorized in that section, the FERC's Order No. 58 seeks to interpret the definition of "first sale" as excluding from the NGPA, almost all gas produced by interstate pipelines (and intrastate pipelines and distributors) themselves, but does not seek to exclude any other gas.[14] The FERC concedes that if its definition is allowed to prevail, the only pipeline produced gas which will be the subject of a "first sale" (and thus subject to NGPA pricing controls) will be that extremely small portion of such gas which is sold so near to the producing well that it is never mixed in a pipeline with gas purchased by the pipeline from other sources. That is a *very* small quantity of gas, since al-

[14] As to gas produced by affiliate producers, the FERC's Interim Regulations which were superseded by Order No. 58, also *excluded all* of that gas from NGPA pricing, by the way "first sale" was *then* interpreted by the FERC, but that interpretation was later totally changed by the FERC in Order No. 58, to *include* such gas. But pipeline produced gas, the FERC claims, in its new contentions, is *still* excluded.

most all gas from all sources is "commingled" in an interstate pipeline for large volume, efficient transportation to market areas. Again, the language of the NGPA does not state, or indicate, any such distinctions within the category of pipeline produced gas, nor does it give the FERC authority to make such distinctions.

The full text of the Section 2(21) definition of "first sale" is as follows:

> (A) General Rule—The term "first sale" means any sale of any volume of natural gas—
>
> (i) to any interstate pipeline or intrastate pipeline;
>
> (ii) to any local distribution company;
>
> (iii) to any person for use by such person;
>
> (iv) which precedes any sale described in clauses (i), (ii), or (iii); and
>
> (v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this Act.
>
> (B) Certain Sales Not Included—Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

In dealing with the above NGPA definition of "first sale", the FERC, in its attempt to achieve its desired result of eliminating NGPA pricing controls over almost all pipeline produced gas, and substituting FERC price controls, was faced with the fact that Subsection A of the definition *includes* as "first sales", the types of sales made by pipelines: to other pipelines (A i), to distributors

(A ii), and to users of gas (A iii). It was also noted that Subsection B then said that such sales "shall not include the sale of any volume of natural gas by an interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, *unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.*" (emphasis added) The underlined phrase is central to these proceedings, since the FERC order which was reversed by the Court below would make such phrase meaningless and surplusage.

The *not* underlined first portion of the above quoted language of Subsection B, which would exclude most sales by pipelines and distributors from "first sales" status, was thus made *not* applicable to gas *produced* and sold by the pipelines and distributors, and their affiliates, by the above underlined "unless" clause, which brings back into "first sale" status, such produced gas. Thus, by the above quoted language of Subsection B, the NGPA provides that:

(i) All gas produced by a pipeline or distributor or their affiliate *is* the subject of a "first sale", when *first* sold, and thus is subject to NGPA prices.

(ii) Gas produced by separate producing companies, which is the subject of a "first sale" when sold by such companies to a pipeline or distributor or user (which is, in fact, the *first* sale of such gas), is *not* the subject of a "first sale" when resold (in a second or subsequent sale) by the pipeline or distributor. (This is necessary, because if the second sale were a "first sale", then there would be two sales under the same price controls, with no provision for the reseller's margin for its costs).

The FERC recognizes and accepts point ii, above, but Order No. 58 classifies only a very small portion of the gas described in point (i) as a first sale, as noted earlier. It does this by asserting that the word "attributable", in the above quoted underlined passage from Subsection B

of Section 2(21) of the NGPA, must be interpreted to mean that if molecules of gas produced by a pipeline or distributor are mixed with molecules of gas from another source, before the pipeline produced gas is sold, then the sale *of such pipeline produced gas* is somehow tainted: it miraculously loses its "first sale" status by allegedly becoming not "attributable to volumes of natural gas produced by such interstate pipeline" under Subsection B. And, the FERC asserts anomalously, the result of such earlier mixing, rather than later mixing, is that the "early mixed" pipeline produced gas is not subject to NGPA price controls, while the later mixed gas and *all other gas* transported in the mixed stream *is* subject to NGPA producer pricing provisions. That interpretation would mean that if a pipeline produced gas from a well and sold that gas to a buyer one hundred yards from the well, it would be a "first sale", but not if it sold both that gas and gas purchased from another producer's interest in the *same well*—even though it delivered all the gas at the *same point*. Such interpretation not only has no support in the statute, but also makes no sense. The Opinion below rejected such tortured interpretation.

4. The Opinion Below

The Court of Appeals rejected the FERC's interpretation of "first sale", and rejected other arguments made by the FERC in Order No. 58, and in the briefs below of Petitioners in these proceedings, all of which attempt to support the FERC's efforts to maintain its pricing authority over the relatively small volumes of pipeline produced gas. The Court held such efforts unsupportable, in the face of the NGPA's clear takeover by the Congress of price controls over all natural gas, to displace FERC (and state) authority. The Court, instead, allowed Congressionally fixed NGPA prices to apply to *all* gas, after finding no indication in the NGPA that Congress intended to—or did—allow the FERC to discriminate as to pipeline produced gas.

SUMMARY OF ARGUMENT

The most basic reasons why Certiorari should not be granted in this case are:

1. This case involves only a narrow, technical question: the interpretation of part of a definition in a statute.

2. The Court of Appeals issued a carefully reasoned decision, which reached a clearly correct result, in which all of the arguments then and now advanced by Petitioners were fully considered.

3. The statutory interpretation adopted by the Court of Appeals does not involve a principle of broad or general applicability: it will affect the revenues of only Respondents and a relatively few other companies. Further, such interpretation does not deal with a continuing question or problem: it is simply a one time classification of now existing, depleting gas reserves of the relatively few companies involved. And the decision of the Court of Appeals provides the governing principle for pricing of pipeline produced gas, until and unless changed by Congress, which the FERC can apply consistently and simply.

4. The result reached by the Court of Appeals is clearly sensible, and it avoids discrimination as between identical categories of gas. It also avoids having substantial legislative and economic results turn on mere corporate form.

5. The statutory interpretation adopted by the Court of Appeals is consistent with the language, intent and limited legislative history of the statute being interpreted. It avoids Petitioners' creation of the unbelievable assumption that a major portion of the definition of "first sale" in the NGPA was inserted by the Congress to deal only with an insignificant quantity of gas: that Congress inserted a special provision in the NGPA so that it would take control over only that tiny *portion* of pipeline produced gas which is sold, uncommingled, offsystem, but wished to give up control over almost all pipeline produced gas, while nevertheless also taking control of *all*

other gas produced by *all* others. That nonsensical pattern, created by FERC claims, is not credible.

6. The decision of the Court of Appeals does not create any regulatory burdens for the FERC, since it adopts processes voluntarily used by the FERC for almost all gas. The Court's decision simply requires full nondiscriminatory use of such processes.

7. The decision of the Court of Appeals carries out the policy of the statute involved: to create a single, Congressionally prescribed, system of pricing controls over all gas, irrespective of the producer thereof, and irrespective of whether the gas ultimately flows in intrastate or interstate commerce.

8. It is doubtful that any decisions exist which are in conflict with the decision below. The single state court opinion which Petitioners allege to be in conflict does not state its basis for decision, so that it cannot be determined if it is conflicting, but that decision has other grounds for decision upon which it could have been, and probably was, based, so that a conflict should not be assumed to exist.

9. The economic effect of the decision below which is alleged by Petitioners is only a small fraction of 1% of the overall cost of natural gas.

REASONS THE PETITIONS SHOULD NOT BE GRANTED

It is important that it be recognized, preliminarily, that this proceeding does not relate to, or prevent, FERC regulation of interstate gas resale and transportation prices: the FERC authority to regulate those prices remains intact, under the Natural Gas Act, under the Court of Appeals' decision below. Thus, the issue here is *not* whether pipeline rates will be unregulated.

Instead, the issue is whether Congress, or the FERC instead, has the authority to fix the prices which must be used as the gas cost component of the overall pipeline rates which the FERC will authorize. Everyone, includ-

ing the FERC and other Petitioners here, agrees that as to the great bulk of the produced gas, the Congress has answered that question and has eliminated the FERC power and responsibility, and has substituted Congressionally fixed, NGPA prices.[15] But Petitioners assert that a narrow exception was created by the NGPA, but *sub silentio*. It will be shown below that such assertion is in error, and would produce unreasonable and discriminatory results, with no gain in regulatory processes and protections. It would result in gas produced from the same wells being subject to widely different prices, depending upon whether the producer is a pipeline, or an affiliate or independent producer, when such distinction is not in the statute and is not based on economic or physical differences.

Petitioners urge, as a basis for their claims, that "forty years" of FERC regulation of the price of pipeline produced gas should not be set aside. But that is fatuous, since it is clear—and not disputed even by Petitioners—that drastic changes to decades of FERC practice is exactly what the Congress intended to accomplish, and did accomplish, in enacting the NGPA. Those dramatic changes—including imposing federal price control on *intrastate* gas, and having *Congress, not the FERC*, set all gas price controls—have been described more fully above. Taking control of intrastate gas pricing away from the states, and control of all independent producer pricing from the FERC, were much larger changes than taking control of pipeline production from the FERC. Thus, it is not even surprising that—as the Court of Appeals found—the NGPA substituted Congressionally fixed prices in place of FERC prices relative to pipeline produced gas, just as it did to *all other* gas. It is incredible to think that it did not, and thus created discrimination between those two categories. The unbelievable character

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[15] The FERC's authority, as to the price of produced gas, is no longer to determine maximum allowable prices, but rather to review prices paid to insure that the Congressionally set "maximum lawful prices" are not exceeded.

of the statutory interpretation by the FERC, which was reversed by the Court of Appeals, is pointed up by the fact that the FERC admits that gas produced by companies affiliated with pipeline companies, even including companies *owned by* pipelines, *must be* priced at NGPA prices, but then contends that the NGPA prices do not apply to gas produced by the pipelines themselves. Thus, the FERC position is that Congress created a substantive distinction, based solely upon corporate *form*, but all without so stating in the statute or legislative history. Such claims are not supportable. The Court of Appeals properly rejected them, as will be shown below. First, however, the narrow nature of these proceedings will be noted.

I. THE OPINION BELOW IS NOT OF BROAD APPLICABILITY OR IMPORTANCE

In addition to the fact, described later, that the decision below is clearly correct, it is also directly relevant here that such decision is not of general, or even broad, applicability, and is not of the order of relative importance which normally occupies the time of this Court.

As shown by the facts stated earlier, these proceedings involve the correct interpretation of a part of a single definition in a federal statute: the NGPA. The FERC contends that its interpretation should be accepted, as a matter of "deference" by the courts. The Court of Appeals, however, considered the FERC views fully, and then exercised judicial expert ability to reach its own interpretation. In Section II, below, that interpretation will be shown to be correct. What is relevant to note here is that the result of the decision below affects relatively little gas, for several reasons. Its effect will be to alter the *rationale* for the prices to be utilized for the relatively small amount of natural gas which is produced by pipeline and distribution companies themselves. But because of action taken voluntarily by the FERC—*i.e.*: allowing NGPA prices for most pipeline produced gas, in exercise

of its alleged discretion—the decision below will, in fact, alter the prices actually received only as to a *small portion* of such limited amount of gas. Therefore, since all gas produced by such companies constitutes only a quite small portion of the natural gas consumed in the nation, the even smaller volume of gas for which the price received will actually be changed by the decision below is an exceedingly small part of national gas consumption. If the annual dollar effect of the decision below which is alleged by the Petition of the FERC is accepted, it constitutes less than one tenth of one percent of the national gas cost. That dollar effect of the opinion below is also a tiny fraction of the multi-billion dollar cost increase created by the NGPA.

The reason that the *rationale* for pricing of almost all pipeline produced gas is changed by the decision below is that such decision reverses the effort of the FERC to interpret the NGPA to allow the FERC to retain price fixing authority over such relatively small amount of gas, even though it is conceded that the NGPA abolishes that authority as to all other gas. The Court of Appeals has held that the language of the NGPA creates no such distinction, and that the legislative history of the act shows no intent to do so.

However, the FERC has itself reduced the practical effect of the decision below, by voluntarily adopting, for application to the largest share of pipeline produced gas, the NGPA prices which the Court of Appeals has required be applied to all such gas. Thus, the actual effect of the decision below is to correct the FERC's erroneous view of its authority over pricing of pipeline produced gas under the NGPA, and to prevent the discriminatory treatment which the FERC would require relative to a *small portion* of such gas. Specifically, in its Order No. 58, the Commission interpreted the NGPA to prescribe Congressionally fixed prices for all natural gas, *except* the bulk of the relatively smaller volumes of gas produced by pipeline companies (and distributors). As to

that "pipeline production", however, the FERC claims that it is not required to allow NGPA prices as the "gas part" of the pipeline's rates, as it is relative to all other gas, but is instead free to "exercise discretion" as to whether or not to use NGPA prices for such purpose. The Commission then undertook to exercise that claimed discretion in its Order No. 98 (App. B-14). In that order, the Commission voluntarily adopted NGPA prices for application to most of the categories of pipeline produced gas which it created, which cover the bulk of the gas produced by pipelines: NGPA prices were allowed to gas which had been priced on area or national rates. Only as to a much smaller portion of pipeline produced gas has the FERC chosen to require different treatment and tried to impose its own pricing system. That portion—gas which was ever priced by the FERC on a "cost of service" basis—is a quite small and finite amount of gas, which is being used up. And no more of such category will be created. Thus, this decision is not of continuing importance: it involves only a one time classification of now existing, finite and depleting, gas reserves.

Accordingly, the volumes of gas which will actually be priced differently as a result of this case is relatively small, and the economic effect will be very small relative to the national cost of gas. The interstate pipeline companies whose gas production will be affected are involved in these proceedings, and the result herein could affect the revenues of only a relatively few other companies. Therefore, this case will not establish principles of general importance or broad applicability, which merit the time of this Court. Instead, the decision of the Court of Appeals has correctly and adequately resolved the narrow issue raised by the incorrect FERC interpretation of the NGPA which is involved herein. Further, the Court of Appeals decision puts to rest a previously recurring issue before the FERC—the process for pricing pipeline production in pipeline rates—so that the question here will not be recurring. Thus, there is no need for action by this Court.

II. THE OPINION OF THE COURT BELOW IS CORRECT

Without fully delineating all bases for the conclusion, as would a brief on the merits, this section will show that the Court of Appeals, below, in a thorough consideration of the opposing views, reached a statutorily correct, and sensible and reasonable, result. In contrast, the FERC position not only has no basis in the statute, but also produces a discriminatory result. It also would violate a basic purpose of the NGPA: the elimination of gas price differentials, between intrastate and interstate sources, and the provision of production incentives. There is no suggestion in the NGPA or its legislative history that the act is to cover only some gas, as Petitioners urge.

A. The Statutory Interpretation And Result Reached By The Court Below Is Correct and Reasonable

This is a case of statutory constitution, involving the interpretation of Section 2(21) of the NGPA. As discussed earlier, it is that section which defines the term "first sale", and the NGPA requires that NGPA prices be applicable to "any first sale" of gas. Section 2(21) states that "first sales" do not include gas sold by pipeline or distribution companies "or any affiliate thereof, *unless* such sale is attributable to volumes of gas produced by such" companies. The Court of Appeals correctly found that such language simply means that there is one "first sale", but only one, of *each* molecule of gas produced. When a producing company—an independent producer or an affiliated producer—sells gas, that is the "first sale" of such gas, and when that gas is resold by a pipeline or distributor which has purchased it, that second sale of such gas is not a "first sale". However, when gas is *produced* by the pipeline or distributor, then the "first sale" of *that* gas is made by such "pipeline producer" or "distributor producer", because they are the producers of that gas.

The above quoted "unless clause" accomplishes that purpose. Sales of gas by the pipeline are *not* first sales

except to the extent that it is volumes of gas produced by the pipeline which are sold: the words of the statute are, "unless such sale is attributable to volumes" of pipeline produced gas. The decision of the Court of Appeals below gives full meaning to all parts of Section 2(21), including the fact that the "unless clause" was inserted for the purpose of covering *all* pipeline produced gas. In contrast, the FERC interpretation calls for the assumption that the "unless clause" covers only some—a *miniscule* proportion—of pipeline produced gas, and such FERC interpretation also means that the statutory provision was inserted for no reason. This is because if, as the FERC claims, the only purpose of the "unless clause" was to include *only* the tiny amounts of "uncommingled" pipeline produced gas as subject to NGPA prices, the statute would simply have left out the "unless clause", thus giving the FERC authority over all pipeline produced gas. The tiny amounts of produced gas which is sold "offsystem", when not "commingled," are too insignificant to have justified a special statutory provision, and had not previously been differentiated by either the FERC or statute.

In contrast, the Court of Appeal's interpretation makes sense of the statute. The "unless clause" is necessary to preserve the symmetry of the statute, to make all gas, including *all* pipeline produced gas, be the subject of one "first sale", but only one. The Court's interpretation also does not produce the discrimination which the FERC position creates. The FERC claims that the NGPA *requires* Congressionally set prices for only the tiny portion of "offsystem, uncommingled" pipeline produced gas, as a matter of law, but *allows* the FERC to use, if it wishes, the same prices for other pipeline produced gas as a matter of FERC "discretion", but to also set its own, FERC created prices, as to another small part of such gas. There are no such distinctions in the statute, and no indication in the statute or legislative history that such a result was intended, or even contemplated. Instead, the language, conference report and other legislative history of the NGPA show that *all* gas is to be subject to the

NGPA pricing provisions, to eliminate dual markets and cost based regulation of produced gas in the interstate market.

The FERC interpretation also demands that another distinction be imagined in Subsection B, where none exists, this one between pipelines and their affiliate producers. That is, the FERC position is that the "unless clause" applies to *all* gas produced by producers which are affiliated with pipelines, but that such clause applies to only some of the gas which is produced by pipelines themselves. But the "unless clause" refers to both pipelines and affiliates, without distinction: thus if it were true, as the FERC claims, that the "unless clause" covers only *some* gas produced by pipelines, then it would cover only *some* gas produced by affiliated producers. But the FERC itself has correctly held that *all* affiliate produced gas is completely covered, which again shows that the FERC interpretation *as to pipeline production* is inconsistent, contrived, without support, and manufactured to attempt to support continued FERC control which was never intended by Congress.

The fact is that the FERC, in Order No. 58, has gone to great lengths to invent an interpretation which would allow it to try to retain control and discretion over the bulk of pipeline produced gas, even though Congress provided to the contrary. And the fact that in Order No. 98, the FERC has exercised its purported discretion to "allow" NGPA pricing to the larger share of pipeline produced gas does nothing to correct the FERC's error in statutory interpretation. As a matter of law, that interpretation is in error, and as a practical matter, if the FERC is allowed to seize the purported discretion which it claims to exist, it could later choose to discriminate against even that larger share of pipeline produced gas as to which, in Order No. 98, it ordered NGPA pricing. It is exactly that discretion, and the lack of incentives and uncertainty which was created, which Congress chose to take away from the FERC, when it enacted the NGPA.

In contrast, the Court of Appeal's interpretation gives equal treatment to all pipeline produced gas, and also gives equal treatment as between gas produced by pipelines, by affiliated producers and by other producers. Petitioners complain that such parity of treatment is inconsistent with the pipeline production practices of the FERC, prior to the NGPA. But they ignore the fact that changing FERC practices is exactly what the NGPA did do, and was intended to do, relative to *all* gas produced: it would be anomalous if the act were interpreted to not do so as to *only* pipeline produced gas. In that regard, the Court of Appeals decision does not, as Petitioners urge, constitute an interpretation that the NGPA "repealed by implication" the former FERC jurisdiction over pricing of pipeline produced gas. Instead, the NGPA *expressly* eliminated FPC pricing jurisdiction over *all* gas produced, by substituting Congressional determination of "just and reasonable prices" (for purposes of the Natural Gas Act) in place of FERC determinations. Thus, cases on "repeal by implication" are not relevant.

Further, the FERC interpretation is not consistent with the goal of the NGPA of providing gas production incentives to all producers. It would be contrary to such purpose to deny NGPA prices, and thus the financial resources and incentives for production which they provide, to pipeline producers. There has been no reason advanced why Congress would have done that. Pipeline production is highly desirable, since the purpose is to provide gas to the pipeline's dependent customers, not to high bidders in other markets. Petitioners note that in Order No. 98, the Commission exercised its claimed "discretion" to provide NGPA price incentives relative to the larger share of pipeline production, but that does not justify the discriminatory failure to do so as to *all* pipeline production. It also points up the fact that the Court of Appeals is correct in its statutory interpretation. The Congress did not allow such FERC "discretion", since there was no reason why Congress would, or should, have relied on the FERC to accomplish what Congress has the authority to do di-

rectly and, in fact, what it did do by the NGPA: providing uniform prices in each gas category, to provide incentives and resources, to *all* producers, to stimulate increased production.

The FERC contentions to the contrary require it to make the extreme interpretation of the NGPA which Petitioners advance, and which the Court of Appeals considered and rejected, including the claim that the term "attributable to" in the Section 2(21) definition of "first sale" means that gas admittedly produced by a pipeline loses its character as pipeline produced gas *if* it is commingled with any other gas *before* it is sold, *but does not do so if* it is commingled *after* it is sold. Such sophistic, meaningless distinctions do not appear in the NGPA. Instead, they are purely creations of the FERC, now supported by Petitioners, to produce the result they desire. Such transparently incorrect statutory interpretation itself strips the FERC of any claim to the "deference" which Petitioners claim that the courts should accord to the FERC's views. In addition, however, it is established law that it is the courts which are expert in statutory interpretation, and that deference to administrative agency statutory interpretation is not required. *SEC* v. *Sloan*, 436 U.S. 103 (1978); *NLRB* v. *Brown*, 380 U.S. 278 (1965); *FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374 (1965); *Herweg* v. *Ray*, 455 U.S. —— (1982), 102 S.Ct. 1059. That is particularly true when, as here, the statute in question produces great changes in prior agency policies and agency practices, and is, in fact, expressly intended to do so, to try to correct adverse results of such prior agency practices. The decision below is consistent with that fact.

> The power of an administrative officer or board to administer a federal statute and to prescribe rules and regulations to that end is not the power to make law—for no such power can be delegated by Congress—but the power to adopt regulations to carry into effect the will of Congress as expressed by statute. A regulation which does not do this, but op-

> erates to create a rule out of harmony with the statute, is a mere nullity (citations omitted).[16]

The cases are legion in which an administrative statutory interpretation has been reversed, where it is inconsistent with statutory language or intent, or with legislative history. An agency may not restrict or enlarge a statute. Since this case involves an effort of the FERC to maintain the authority which Congress has taken from it, the principle which is most applicable is that reversal is obviously needed where an "agency's interpretation departs from the statutory mandate that it is explicable more easily as an organic reflex *to extend its own jurisdiction than as a reasoned interpretation of the statute.*" *Usery* v. *First National Bank of Arizona*, 586 F.2d 107, 111 (9th Cir. 1978) (emphasis added).

Finally, the Court of Appeals also avoided the above described discrimination between identical gas. That discrimination would make the statutory provision in issue here invalid, *if* the statute were interpreted to produce such result. *Schneider* v. *Rusk*, 377 U.S. 163, 168 (1964); *Curren* v. *Wallace*, 306 U.S. 1 (1938).[17]

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[16] Manhattan General Equipment Co. v. Comm'r of Internal Revenue, 297 U.S. 129, 134 (1936). Consistently, Section 501 of the NGPA, 15 U.S.C. § 3411(b), gives the FERC authority to define only "accounting, technical and trade terms"—which the term "first sale" is not—and then only "consistent with the definitions set forth in this Act." *See* Int. Bhd. of Teamsters, etc. v. Daniel, 439 U.S. 551, 568 n.20 (1979); Shea v. Vialpando, 416 U.S. 251 (1974); Morton v. Ruiz, 415 U.S. 199 (1974); Espinoza v. Farah Mfg. Co., 414 U.S. 86 (1973); Fed. Mar. Comm'n v. Seatrain Lines, Inc., 411 U.S. 726, 745 (1973); Volkswagenwerk Aktiege v. Fed. Mar. Comm'n, 390 U.S. 261, 272 (1968); NLRB v. Brown, 360 U.S. 278, 291 (1965); Davies Warehouse Co. v. Bowles, 321 U.S. 144 (1944); Neuberger v. Comm'r, 311 U.S. 83 (1940).

[17] Such discriminatory result would also mean that Section 270.203 is (1) "contrary to constitutional right, power (and) privilege . . ."; and (2) "in excess of statutory jurisdiction, authority, or limitations or short of statutory right," in violation of Sections 706(2)(A), 706(2)(B), and 706(2)(C), of the Administrative Procedure Act, 5 U.S.C. §§ 706(2)(A)-706(2)(C), as well as the NGPA. The

B. The Decision Below Creates No Regulatory Problems For The FERC Or State Regulation

The FERC and state regulatory agencies each fix the sales rates of the pipelines and distributors which they regulate, by adding to the transportation, sales, administrative and financial costs of those companies, a value for the gas which they sell. This produces the "cost of service" upon which rates are based. The value for gas *purchased* by pipeline companies is the price paid for such gas, which in turn is largely subject to government control. Prior to the NGPA, those agencies also used as the value for much of the gas *produced* by pipeline companies, those prices fixed by government for the sale of gas by independent producers and affiliated producers. Use of such unit prices was frequently required by the FERC. *Subsequent* to the NGPA, those agencies, including the FERC, have *continued* to use governmentally set maximum lawful prices—which are now NGPA, Congressionally set, prices—as such values for the larger share of such pipeline and distributor produced gas. Thus, the FERC and state agencies cannot claim that any burden, or regulatory gap or problem, will be created by the decision below requiring them to use the *same*

FERC orders here are also in violation of the principles of United States Dept. of Agriculture v. Moreno, 413 U.S. 528 (1973) and Community-Service Broadcast of Mid-America, Inc. v. FCC, 593 F.2d 1102 (D.C. Cir. 1978) (cited at FERC Order No. 102 (App. B-50), here under review, at 14 n.20). Such cases held statutes unconstitutional because they imposed classifications which were not reasonably related to a legitimate government interest and/or narrowly tailored to a substantial government interest. In the present case, it has been shown that the Congress, in the NGPA, did not classify pipeline production separately from other natural gas production, and that the aim of the relevant parts of the NGPA is to establish a uniform pricing policy and to stimulate gas production. Exclusion of pipeline producers from NGPA pricing provisions contradicts such goals. Thus, the legitimate government interest here is defeated by the FERC's interpretation, so that either the interpretation or the statutory section must fall. In this case, it is obviously the interpretation which is in error.

procedures as to *all* such produced gas.[18] Indeed, that is the simplest, least burdensome process.

Those agencies will simply continue to price all *gas*—whether produced by the pipeline or distributor, or pur-

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[18] Petitioners assert that the FERC must retain the selective discretion which it claims, so as to be able to require Respondents to use "cost based" prices (cost of service method) for certain of the gas produced by Respondents, alleging a windfall will otherwise occur. This is the same "windfall" claim made by some Petitioners against the NGPA itself, but Congress passed the Act anyway: the case here is another effort to argue against the policy of the Act. The windfall claim is also factually in error on several bases, in addition to its legal invalidity, described earlier. First, the gas to which the FERC would apply its selective pricing scheme is said to be from wells which at one time or another were subject to cost based pricing. In fact, a substantial proportion of gas produced by independent producers was also regulated by the FERC's predecessor on a cost service basis, but the FERC makes no attempt to continue to regulate *that* gas on a cost basis: it voluntarily gave up such efforts years ago. Further, there is no certainty or uniformity as to whether such cost of service treatment was, in individual situations, more or less beneficial than the then alternative "area rates": the FPC itself has acknowledged it was sometimes less beneficial. Nat'l Fuel Gas Supply Corp., FPC Docket No. RP76-96, 18 FPS 5-829 (1979). Thus, no *post hoc* "correction" for such treatment is justified, needed or possible. Further, not all the gas which the FERC asserts to be in the category which it believes to now require such disparate treatment is actually in such category. For example, Respondent Michigan Wisconsin Pipe Line Company, in the time period when it did not receive the FERC's required area rate pricing, received cost allowances for its own produced gas which were less than its actual costs overall, and recovered full costs only one year out of seven, again showing that the FERC's erroneous interpretation of the NGPA would not, and is not needed to, correct alleged past inequities or present alleged windfalls: that rationale is as fallacious as is the statutory interpretation proposed by the FERC and rejected by the Court of Appeals. Finally, companies which would be denied NGPA prices by the FERC, if the decision below is not reversed by the Court of Appeals, would have been those with gas from leases which had *ever* received cost of service pricing. Since such treatment was often *imposed* on companies, there is no similarity to the limits imposed by "optional certificate conditions", as urged by the FERC petition herein.

chased by them—at Congressionally fixed NGPA prices (or competitively set comparable prices) and will add the other costs of rendering service, to compute the overall cost of service. That is how the rates for all sales of gas will continue to be calculated. In fact, uniform use of NGPA prices, as the Court of Appeals has required, will reduce regulatory burdens, since there will be no gas as to which the regulatory agencies will be required to hold hearings to determine its cost of production.[19]

In that context, it may be seen that the major technical attack made by Petitioners on the decision below is irrelevant. Each pipeline sells, to its customers, the gas which it produces and purchases. With sales of the gas which the pipeline itself produces held to be the "first sale" of such gas, the regulation of pipeline rates, and the values fixed for the cost component thereof, will be just as described above: the NGPA prices will be the value used for the gas component of pipeline rates, to which will be added all other costs, to achieve the overall "cost of service". The Court of Appeals produced exactly the same result by deeming, for purposes of Section

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[19] The fact that the Commission has chosen to use NGPA prices for most pipeline produced gas does not moot this appeal, since it has refused to do so as to some gas. As the Court of Appeals correctly observed, in the decision below: "The fact that the agency gives back all or part of what it takes from the law's grant in no way justifies departure from the congressional purpose in the first instance." Further, the fact that there are no contracts which relate to pipeline produced gas, and thus no "contract limits", as raised by Petitioners, is a red herring. That is also true as to the pipeline produced gas to which the FERC chooses to award NGPA prices, despite the absence of contracts. Further, contracts between producers and their affiliated purchasers can be freely amended, but NGPA prices apply. In fact, consumer protection is provided by the NGPA, pursuant to which comparable competitive prices govern as to gas deregulated by the NGPA, while Section 601 of the NGPA serves to prohibit "first sales" by a pipeline to an affiliate, or vice versa, from being at prices higher than those in comparable sales between non-affiliates. Accordingly, claims that the opinion below leads to loss of consumer protection are also in error.

2(21) of the NGPA, the "first sale" to be the transfer of the pipeline produced gas from the producing facilities and operations of the pipeline to the transportation facilities and operations. Under such conceptualization, the regulatory processes—and rates—will be exactly the same as described earlier. The same values apply to the gas itself—produced or purchased—and they are added to the same other pipeline costs to produce the same overall pipeline rates. Thus, there are no differences in processes or results produced, irrespective of *when* the "first sale" occurs.

Accordingly, Petitioners' major claim is irrelevant. They argue that the intra-company transfer is not a "true" sale and thus cannot be a "first sale". Such position is refuted by the Court of Appeals decision. In that regard, it should be noted that such "transfers" are required to be treated as sales by Federal Accounting Standard Board rules: the production division of pipelines keep separate records, and record sales income when gas which they produce is transferred to the pipeline division, in accounting for their profits and losses.[20]

But even more importantly, even if it were assumed, *arguendo*, that the Court of Appeals was incorrect when it deemed the first sale to be at the above described transfer point, as Petitioners urge, on the grounds that such transfer is not a "true" sale, the claims made and results advocated by Petitioners must nevertheless be rejected as erroneous because there are subsequent "true sales" by each pipeline, to its distribution company and user customers, under *any* definition of sale. Thus, Petioners are able to advance their claims only because they also ignore those "true" sales which are, without dispute,

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[20] See also Amoco Production Co., *et al.* v. DOE, *et al.*, U.S. District Court for the District of Delaware, Dkt. Nos. Civil 78-463, *et al.*, April 9, 1981 (Federal Energy Guidelines, p. 28,460), where it was held that transfers of oil between divisions and affiliates are "first sales" under the regulations pursuant to the Emergency Petroleum Allocation Act of 1973.

made by pipelines, and thus clearly qualify as "first sales" (if it were assumed the earlier sale found by the Court does not qualify). Further, irrespective of which interpretation of the exact point of sale is adopted, the results produced by Petitioners' theories are unsupported and not reasonable, for the reasons stated in preceding sections hereof: those theories are equally invalid under either choice of the point at which the "first sales" occur. It is neither necessary nor productive for this Court to spend its energies simply to specify the theory upon which the Court of Appeals is to be upheld.

Finally, the suggestion of one Petitioner that the Court of Appeals erred because it reversed Order No. 98, is clearly in error. That Order rests wholly upon the FERC's assumption that it has discretion to deny NGPA pricing, whereas it does not, as the Court of Appeals held. Such holding automatically requires reversal of Order No. 98, as well as Order No. 58.

III. THE BASIS FOR DECISION OF THE ALLEGEDLY CONFLICTING DECISION CANNOT BE DETERMINED SO THAT NO CONFLICT CAN BE FOUND

Petitioners allege that the decision below is in conflict with a decision of the West Virginia Supreme Court in *Pennzoil Company* v. *Pub. Serv. Comm'n of West Virginia* (1981).[21] In fact, however, it is clearly doubtful that such a conflict exists, since there were several unrelated grounds upon which the West Virginia Court could have, and was asked to, base its decision, including "threshold" bases upon which the decision probably was founded. That Court did not state the basis for its decision, but instead, in a one page order,[22] simply affirmed

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[21] No. 80-175-G-42T (Dec. 10, 1981). Pennzoil has sought certiorari: Petition of March 10, 1982, 50 U.S.L.W. 3768 (No. 81-1672).

[22] That order is set forth in Appendix A to Pennzoil Company's petition for certiorari in No. 81-1672 at 1a.

an order of the West Virginia Public Service Commission. There is, of course, no indication in the West Virginia Supreme Court decision that such Court even considered, much less rested its decision upon, the question involved here: whether the NGPA requires use of NGPA prices for gas produced by pipelines and distribution companies.

Petitioners point out that the West Virginia Supreme Court *could have* based its decision on such grounds, had it desired to do so, since the West Virginia Public Service Commission, in the decision affirmed, ruled on that issue. But that Commission also relied upon three other grounds for its decision, so that it is impossible to determine the basis for the West Virginia Supreme Court order, since it mentions none of the grounds. Those other grounds include the West Virginia Commission's position that it has full authority over distribution rates under Section 602 of the NGPA, irrespective of the definition of "first sale" or the applicability of NGPA prices to gas produced by distribution companies; the claim that Pennzoil must, and was not able to, show that the "end result" which the Commission's decision achieved failed to provide good service at fair rates to consumers, and a competitive return to Pennzoil, irrespective of regulatory methods and findings; and the claim that Pennzoil did not exhaust its administrative remedies because it did not seek rehearing from the Commission. Those grounds, upon any one of which the West Virginia Supreme Court may have rested its affirmance, have been summarized by the West Virginia Commission before this Court.[23] The fact that those grounds exist, but that none were mentioned by the Court, means that it is not possible to determine that there is any conflict between

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[23] In its brief in opposition to the petition for certiorari in No. 81-1672 in this Court. The decision of the West Virginia Public Service Commission is printed as Appendix B to that brief.

the decision below and the West Virginia *Pennzoil* decision. Accordingly, none should be *assumed*.

The West Virginia Public Service Commission has stated, in these proceedings, that no conflict exists between the decision below and the West Virginia *Pennzoil* decision.[24] That statement is presumably based, at least in part, on a conclusion that the West Virginia Supreme Court should have, and presumably did, apply the well founded principle that affirmance should be on narrow threshold issues, and on state grounds, rather than upon seminal interpretations of federal statute, where possible. In any event, there is no basis for a finding that the *Pennzoil* decision does conflict with the decision below, because it is unlikely, and in no event certain, that the Pennzoil decision even considered, much less relied upon, the pipeline and distributor gas production principles which are involved in these proceedings.[25]

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[24] *See* "Response of the Public Service Commission of West Virginia to the Motion of Arizona Electric Power Cooperative, Inc., for Contemporaneous Consideration and Disposition of Petitions for Certiorari", dated April 29, 1982, filed in Arizona Electric Power Cooperative v. Mid-Louisiana Gas Co., No. 81-1958.

[25] Under such circumstances, it also appears appropriate that the *Pennzoil* decision be summarily remanded for clarification of the West Virginia Supreme Court's affirmance, and possible reconsideration in light of denial of certiorari herein.

CONCLUSION

Because the petitions for writ of certiorari herein present no significant reasons for review, and because the decision below is not of general or broad significance, and is correct, such petitions should be denied by this Court.

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August 4, 1982

Opposition

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Nos. 81-1889, 81-1958, 81-2042 and 82-19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*,
Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Petitions for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

---

BRIEF OF RESPONDENT KENTUCKY WEST VIRGINIA GAS COMPANY IN OPPOSITION

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QUESTION PRESENTED

Whether the opinion below correctly found that the plain language, purposes and legislative history of the Natural Gas Policy Act of 1978 show that Congress intended that natural gas production attributable to an interstate pipeline or local distribution company be subject to the national pricing program established by that Act?

LISTING OF AFFILIATES PURSUANT TO RULE 28.1

Listed below, pursuant to Rule 28.1 of the Rules of the Supreme Court of the United States, are the parent, subsidiaries and affiliates of Respondent Kentucky West Virginia Gas Company:

Berea Gathering Company
Equitable Gas Company
Equitable Gas-Energy Company
Kentucky Hydrocarbon Company
Kepco, Inc.
Philadelphia Oil Company

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	(i)
LISTING OF AFFILIATES PURSUANT TO RULE 28.1	ii
TABLE OF AUTHORITIES	iv
COUNTERSTATEMENT OF THE CASE	2
I. Regulatory Structure Under the Natural Gas Act	2
II. The Natural Gas Policy Act	6
III. Proceedings Below	7
REASONS FOR DENYING THE WRIT	10
I. Summary of Argument	10
II. Argument	11
A. The Court Below Properly Interpreted the NGPA	12
1. The Court of Appeals Correctly Found that the Commission Regulations Under Review Failed to Recognize an Express Requirement of the NGPA	12
2. Congress Did Not Intend in the NGPA to Continue Cost-Based Regulation of Pipeline Production	13
3. The NGPA Clearly Contemplates that Pipeline and Distribution Company Production Should Be Subject to the NGPA Pricing Program Applicable to "First Sales"	19
B. Assertions of the Economic Impact of the Court of Appeals Decision Do Not Warrant Review	24
C. There Is no Reason to Presume a Conflict Between the *Mid-Louisiana* and *Pennzoil* Decisions When a Conflict Is Not Apparent	25
CONCLUSION	27

TABLE OF AUTHORITIES

Cases:	Page
Federal Election Comm'n v. Democratic Senatorial Campaign Comm., 102 S.Ct. 38 (1981)	19
FMC v. Seatrain Lines, Inc., 411 U.S. 726 (1973)	19
FPC v. Hope Natural Gas Co., 320 U.S. 591 (1944)	2
FPC v. Tuscarora Indian Nation, 362 U.S. 99 (1960)	19
Gillring Oil Co., 20 F.P.C. 770 (1958)	3
Hugoton-Anadarko Area Rate Proceeding, 31 F.P.C. 1585 (1964)	4
Just and Reasonable National Rates for Sales of Natural Gas, 52 F.P.C. 1604 (1974), *aff'd sub nom. Shell Oil Co. v. FPC*, 520 F.2d 1061 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976)	4, 5, 16
Monrosa v. Carbon Black, Inc., 359 U.S. 180 (1959)	26
Panhandle Eastern Pipe Line Co., 25 F.P.C. 787 (1961), *aff'd*, 305 F.2d 763 (D.C. Cir. 1962), *cert. denied*, 372 U.S. 916 (1963)	3
Pennzoil Co. v. Public Serv. Comm'n of West Virginia, No. 80-175-6-42T (W. Va. Dec. 10, 1981), *petition for cert. filed*, 50 U.S.L.W. 3768 (U.S. Mar. 23, 1982) (No. 81-1672)	11, 25, 26
Permian Basin Area Rate Proceeding, 34 F.P.C. 159 (1965), *aff'd, Permian Basin Area Rate Cases*, 390 U.S. 747 (1968)	3, 4
Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672 (1954)	3
Pipeline Production Area Rate Proceeding, 35 F.P.C. 497 (1966)	4
Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738 (1969), *aff'd sub nom. City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972)	5, 16
Statement of General Policy No. 61-1, 24 F.P.C. 818 (1960)	3

TABLE OF AUTHORITIES—Continued

Statutes:	Page
Natural Gas Act, 15 U.S.C. §§ 717-717w	*passim*
Section 1, 15 U.S.C. § 717(b)	3
Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-3432	*passim*
Section 2(21)(A), 15 U.S.C. § 3301(21)(A)	7
Section 2(21)(B), 15 U.S.C. § 3301(21)(B)	*passim*
Section 102, 15 U.S.C. § 3312	7
Section 103, 15 U.S.C. § 3313	7
Section 104, 15 U.S.C. § 3314	7
Section 105, 15 U.S.C. § 3315	7
Section 106, 15 U.S.C. § 3316	7
Section 107, 15 U.S.C. § 3317	7, 23
Section 108, 15 U.S.C. § 3318	7, 23
Section 109, 15 U.S.C. § 3319	7
Section 203(a)(1)-(8), 15 U.S.C. § 3343(a)(1)-(8)	22
Section 203(b)(2), 15 U.S.C. § 3343(b)(2)	22
Section 501(b), 15 U.S.C. § 3411(b)	20, 21
Section 601(b)(1)(E), 15 U.S.C. § 3431(b)(1)(E)	18

Miscellaneous:	
Breyer & MacAvoy, *The Natural Gas Shortage and the Regulation of Natural Gas Producers*, 86 Harv. L. Rev. 941 (1973)	3
124 Cong. Rec. 38,361 (1978)	15
H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983	7, 14, 21
Staff of Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 2d Sess., Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978 (Comm. Print 95-62) (1978)	15

IN THE

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Respondents.

On Petitions for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

---

BRIEF OF RESPONDENT KENTUCKY WEST VIRGINIA GAS COMPANY IN OPPOSITION

As a respondent, Kentucky West Virginia Gas Company ("Kentucky West") opposes the petitions for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit filed by the Public Service Commission of the State of New York ("New York"), in No. 81-1889, Arizona Electric Power Cooperative, Inc. ("AEPCO") in No. 81-1958, the State of Michigan ("Michigan") in No. 81-2042, and the Federal Energy Regulatory Commission ("Commission" or "FERC") in No. 82-19.[1]

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[1] Pursuant to Rules 22 and 34.2, Kentucky West adopts the portions of the Petition filed by New York in response to Rule 21.1(b), (d), (e) and (f). All appendix citations herein refer to the appendix filed by New York in No. 81-1889.

COUNTERSTATEMENT OF THE CASE

I. Regulatory Structure Under the Natural Gas Act

In their "Statements of the Case" both the FERC (Pet. at 4) and New York (Pet. at 4) state that regulation of pipeline production under the Natural Gas Act ("NGA"), 15 U.S.C. §§ 717-717w (1976), followed a different course than that of independent producers. Kentucky West submits that whatever differences existed between the regulation of the wellhead prices applicable to independent producer, pipeline and pipeline affiliate production, those differences are as described in this "Counterstatement of the Case."

When interstate pipelines were first made subject to federal regulation under the NGA, the Federal Power Commission and its successor, the FERC, were required and empowered to set "just and reasonable" rates for the interstate transportation and sale for resale of natural gas by a pipeline. *See FPC v. Hope Natural Gas Co.*, 320 U.S. 951 (1944). In setting "just and reasonable" pipeline rates, the Commission determines a "cost of service" for an individual pipeline company for a representative period. *Id.* Generally speaking, costs incurred by a pipeline consist of the following:

> a. The various costs incurred to operate and maintain the pipeline, and to administer and finance it, including the cost of depreciation, debt service and an allowance for return on equity capital and associated income taxes.
>
> b. The cost of natural gas which is purchased from others and resold by the pipeline (purchased gas).
>
> c. The cost of, or value attributed to, natural gas which the pipeline or an affiliate produces from gas reserves which it owns and sells to its customers.

This case concerns the proper manner of calculating category (c) in light of the Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. §§ 3301-3432 (Supp. IV 1980).

Prior to the NGPA, one method the Commission utilized to determine the rate for pipeline produced gas was the individual pipeline cost of service method, in which the Commission determined the cost of service for pipeline production in a manner similar to the cost of service methodology used to determine a pipeline's transmission costs. *See, e.g., Panhandle Eastern Pipe Line Co.*, 25 F.P.C. 787, 794 (1961), *aff'd*, 305 F.2d 763 (D.C. Cir. 1962), *cert. denied*, 372 U.S. 916 (1963). As further described below, the Commission subsequently changed to area and national rate methodologies for setting the rates of certain gas produced by pipelines.

In *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672 (1954), this Court held that independent producers that sell natural gas for resale in interstate commerce are "natural gas companies" within the meaning of Section 1 of the NGA. 15 U.S.C. § 717(b). As a result, independent producers were made subject to the Commission's NGA ratemaking jurisdiction. Consequently, the Commission attempted to determine an individual producer's cost of service including a fair rate of return for the sale of natural gas by the producer. *Permian Basin Area Rate Cases*, 390 U.S. 747, 756 (1968); *Gillring Oil Co.*, 20 F.P.C. 770 (1958). The methodology first employed was similar to that used to regulate rates for the sales of natural gas produced by interstate pipelines.[2] However, in light of the difficulties and administrative burdens in applying the cost of service methodology to the vast numbers of independent producers,[3] the Commission in 1960 initiated proceedings[4] to establish maximum producer rates for each of the major producing areas. Under this method, average industry-wide costs including dry

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[2] *See* Breyer & MacAvoy, *The Natural Gas Shortage and the Regulation of Natural Gas Producers*, 86 Harv. L. Rev. 941, 952-53 (1973).

[3] *See* Permian Basin Area Rate Cases, 390 U.S. at 757 n.12 (1968).

[4] Statement of General Policy No. 61-1, 24 F.P.C. 818 (1960).

hole and other exploratory costs were computed for a particular region to which was added a rate of return allowance to determine the price that independent producers could charge for production from that region.[5] Subsequently, the Commission adopted national rather than area rates. Both the area and national rates included a rate of return that was based on returns allowed to interstate pipelines engaged in the transportation of natural gas, plus an increase in the rate of return "to take fully into account the greater financial risks of exploration and production." *Permian* 390 U.S. at 762. Additionally, in establishing national rates for independent producers, the Commission included the cost of drilling unsuccessful wells ("dry hole cost") in the rate base, with the producers consequently earning a return on these costs. *Shell Oil Co. v. FPC*, 520 F.2d 1061, 1069 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976). Thus, in determining both area and national cost of service rates, independent producers received an allowance for unsuccessful drilling efforts as well as a higher rate of return to take into account the greater risks of exploration and production.

Shortly after the Commission determined to shift from individual to average area costs for determining the rates for independent producers, it initiated consideration of whether interstate pipeline and pipeline affiliate production of natural gas (previously regulated on an individual company cost of service basis) should also be regulated on the basis of area rates. *Hugoton-Anadarko Area Rate Proceeding*, 31 F.P.C. 1585 (1964). The pipeline and pipeline affiliate production issue was severed from this proceeding, and a new inquiry was instituted that required any final decision to be applied prospectively. *Pipeline Production Area Rate Proceeding*, 35 F.P.C. 497, 499 (1966). Following extensive hearings, the Commission in 1969 finally spoke to the issue, de-

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[5] Permian Basin Area Rate Proceeding, 34 F.P.C. 159, 192-93 (1965), *aff'd*, Permian Basin Area Rate Cases, 390 U.S. 747 (1968).

termining that it would prospectively value pipeline and pipeline affiliate production at the wellhead using the same area rate methodology utilized for independent producer production of natural gas, while individual company cost of service treatment would continue for pipeline and pipeline affiliate production from leases acquired prior to its decision. *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738 (1969), *aff'd sub nom. City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972). The Commission rejected the suggestion that the effective date of pipeline area rates should be retroactive to the date independent producer area rates became effective, because the original order issued in 1966 required that any decision respecting pipeline production was to apply to production from after-acquired leases "in order to expedite the proceedings and to avoid complications and evidentiary problems," and that to now change the effective date "would introduce issues that were not previously involved." *Id.* at 753. Significantly, the Commission noted that the same "basic incongruities" presented in fixing independent producer prices on an individual cost of service basis apply equally to pipeline production, and that this methodology has led to a "continuing reduction in the relative amount of pipeline production." *Id.* at 746-47. The Commission subsequently determined in Opinion No. 699-H that pipeline and pipeline affiliate production from wells commenced after January 1, 1973, regardless of lease acquisition date, would be valued at the same just and reasonable nationwide rates applied to independent producers. *Just and Reasonable National Rates for Sales of Natural Gas*, 52 F.P.C. 1604, 1656 (1974), *aff'd sub nom. Shell Oil Co. v. FPC*, 520 F.2d 1061 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976).

Significantly, under the NGA, the Commission treated production by an affiliate of a pipeline in the same manner as production by a pipeline. *City of Chicago*, 458 F.2d at 737 n.20. That is, the individual company cost of service methodology was used for pipeline and affiliate

production from leases acquired or wells commenced before a particular year, while the area or national cost of service method was used for pipeline or affiliate production from leases acquired or wells commenced after that year.

The foregoing traces the Commission's use of cost-based ratemaking concepts under the NGA, by first utilizing the individual company cost of service methodology and then shifting to area or national cost of service in determining natural gas prices. Both the individual company cost of service and the area and national cost of service concepts were applied under the NGA to independent producers, pipeline affiliate producers, *and* pipeline producers, although the year the Commission implemented such methodology to independent producers or to pipeline and pipeline affiliate producers differed as set forth above. This timing difference was not that significant from the standpoint of the costs borne by consumers. With respect to both area or national cost of service regulation and individual company cost of service regulation, the Commission purported to permit recovery of dry hole and other exploratory costs and to set rates of return taking into account the risks of exploration and production operations.

The fundamental consideration for Congress at the time of the NGPA's enactment, was whether or not the existing pattern of cost-based regulation (whether individual company, area or national cost of service) should be continued or whether a new national pricing program for natural gas should be established.

II. The Natural Gas Policy Act

The NGPA was one of several statutes enacted in 1978 to deal with the Nation's growing energy shortage. The essential purpose of the NGPA was to establish a national and uniform natural gas pricing policy so as to assist and stimulate the production of natural gas.[6]

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[6] The Joint Explanatory Statement of the Committee on Conference accompanying the NGPA stated that "[t]he natural gas pricing

This goal was to be effectuated by legislative mandate of increased prices to producers of natural gas. Through the NGPA, Congress generally abandoned the cost-based regulatory approach of the Natural Gas Act respecting natural gas production, and substituted a statutory price control formula applicable to both intrastate and interstate natural gas sales. This formula relies upon a system of classifying and pricing categories of gas based upon the circumstances of its production and sale.[7]

The maximum lawful prices established by Title I of the NGPA apply to "first sales" of natural gas, which are defined in Section 2(21)(A) as any sale *to* any interstate or intrastate pipeline, distribution company, or end user. 15 U.S.C. § 3301(21)(A) (Supp. IV 1980). This broad definition of "first sale" is then narrowed in Section 2(21)(B) so as to exclude sales made *by* an interstate or intrastate pipeline, distribution company or affiliate thereof "unless such sale is attributable to volumes of natural gas produced" by such an entity. *Id.* § 3301(21)(B). The issue in this case is whether natural gas produced and sold by an interstate pipeline is a "first sale" within the contemplation of the NGPA and therefore subject to the maximum lawful prices established in Title I of the NGPA.

III. Proceedings Below

The Commission in Order No. 58 promulgated final regulations interpreting the Congressional definition of "first sale" thereby controlling the price at which natural

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policy passed by the House as Part 4 of H.R. 8444 . . . established a single uniform price policy for natural gas produced in the United States. H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 67, *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983, 8984. Title I of the NGPA as enacted tracked Part 4 of H.R. 8444, with changes which in no way detract from the intent to establish a uniform gas pricing policy.

[7] The various categories are set forth in Sections 102-109 of Title I of the NGPA. 15 U.S.C. §§ 3312-3319 (Supp. IV 1980).

gas produced by interstate pipeline companies may be sold.[8] The FERC recognized the right of independent producers and pipeline affiliates to collect NGPA prices for the sale of their natural gas production, but held that interstate pipelines are not subject to NGPA prices for gas they produce if such gas is mixed with gas purchased from others prior to sale. In this manner the FERC reserved to itself the authority to continue cost of service regulation of a pipeline's natural gas production even though production of natural gas by independent and pipeline affiliate producers was subject to the NGPA pricing program. The Commission interpreted the word "attributable" set forth in the Congressional definition of "first sale," as meaning that the volumes must be "comprised exclusively" of gas produced by the pipeline, rather than employing the ordinary meaning of "attributable." The FERC justified this interpretation of "first sale" based on allegations that "commingled" gas is not in any manner "attributable" to a pipeline's own production, and that it intruded the least into state regulation and was less difficult to administer. *See, e.g.*, App. at B-2, B-4, B-5.

The Commission also determined in Order No. 58 that all sales of natural gas by an affiliate of an interstate pipeline are "first sales" and thus entitled to NGPA pricing. Notably, although pipeline and pipeline affiliate production were treated the same under the NGA, and Section 2(21)(B) of the NGPA treats pipeline and pipeline affiliate production jointly and in the conjunctive, the FERC in Order No. 58 determined that all pipeline affiliate production will be treated as a "first sale," while only the relatively small volume of pipeline production which is not "commingled" with purchased gas is entitled to "first sale" treatment.

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[8] Order No. 58, Final Rule Governing the Maximum Lawful Price for Pipeline, Distributor or Affiliate Production, Docket No. RM80-7 (Nov. 14, 1979). App. B-1 to B-13.

The Commission subsequently issued Order No. 98 which promulgated regulations under the Natural Gas Act governing the wellhead price of interstate pipeline production sold in mixed volume or "commingled" sales.[9] The regulations permit, as a matter of Commission *discretion*, pipeline production previously priced on an area or nationwide basis to be priced at the level that would have been applicable under Title I of the NGPA if such sales were "first sales." Conversely, pipeline production previously priced on a cost of service basis would not be subject to the pricing provisions of the NGPA, but would continue to be subject to FERC cost of service regulation under the NGA.

On review of Order Nos. 58 and 98, the court in a unanimous decision below held that the language, purpose and legislative history of the NGPA required the conclusion that Congress "clearly intended" that any production attributable to an interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, is to be accorded "first sale" status under the NGPA and is thus governed by the comprehensive pricing scheme of that Act. The court found that the Commission's interpretation "would render the unless clause of [Section 2(21)(B)] a nullity" and would effectively read this clause out of the NGPA. App. at A-8. Moreover, the court held that nothing in the language of the NGPA "suggests any intent to deny NGPA pricing to natural gas just because it is produced by a pipeline." App. at A-8, A-9. Consequently, the court vacated the FERC's Order No. 58 as inconsistent with the express language of the NGPA and the Congressional intent and purpose, and vacated Order No. 98 because the Commission lacked authority to set prices for interstate pipeline production under the Natural Gas Act. The court found it unnecessary to reach Kentucky West's alternate claim that, if

[9] Order No. 98, Final Rule Governing Pricing of Pipeline Production Under the Natural Gas Act, Docket No. RM80-6 (Aug. 4, 1980). App. B-14 to B-49.

the Commisison retained jurisdiction under the NGA to establish the price of pipeline produced gas, it abused its discretion in Order No. 98 by discriminatorily applying cost of service pricing to pipeline production while independent and pipeline affiliate production were subject to the NGPA's national pricing program. App. at A-2.

New York filed a timely application for rehearing of the opinion below issued December 23, 1981, and suggestions for rehearing *en banc* were filed by Michigan and AEPCO. By order of February 5, 1982, the applications for rehearing or rehearing *en banc* were denied. New York also filed a motion with the court below for stay of the mandate, which was denied by order of March 2, 1982. Subsequently, New York, Michigan, AEPCO, and the FERC filed petitions for a writ of certiorari with this Court.

REASONS FOR DENYING THE WRIT

I. Summary of Argument

Petitioners have failed to establish a basis for this Court to exercise its extraordinary and discretionary jurisdiction to grant a writ of certiorari. The decision below involves a straightforward question of statutory construction which was properly decided by a unanimous opinion of the Court of Appeals, after full consideration of the issues, and consistent with established principles of interpretation. Based on the plain language, legislative intent and history, the decision below properly vacated the Commission's discriminatory application of the NGPA pricing program to independent and pipeline affiliate producers but not to pipeline producers.

It is clear that the purpose and intent of Congress in passing the NGPA was to remove the pricing of gas production from the cost-based regulatory methods used by the FERC and to substitute a Congressionally determined national price structure. The decision below does not, as Petitioners argue, remove regulatory jurisdiction

over pipeline or distributor sales to their customers, but simply recognizes the plain intent of Congress that the price of gas attributable to production by a pipeline or distributor be governed by the prices provided in the NGPA. The Court of Appeals recognized the fundamental change in national policy respecting the pricing of natural gas production, and struck down the FERC's anomalous interpretation which would have continued cost-based regulation under the NGA over most pipeline production and resulted in irrational discrimination between producers of natural gas from the same fields and wells based solely on corporate organization, *i.e.*, whether the producer was an interstate pipeline rather than an independent producer or affiliate of an interstate pipeline.

Notably, the FERC regulations vacated by the court were not based on administrative expertise or experience with the statute, but were an initial effort to continue what the Commission, not Congress, thought to be a desirable economic policy (continued cost-based regulation of pipeline production), a policy clearly rejected by Congress in the national pricing plan established by the NGPA. Consequently, assertions by Petitioners and Amici of economic impact should be presented to Congress and do not provide a basis for granting certiorari. Finally, as shown, *infra*, there is no reason to presume a conflict between *Mid-Louisiana* and *Pennzoil Co. v. Public Serv. Comm'n of West Virginia* [10] when a conflict is not apparent.

II. Argument

Petitioners contend that the holding of the Court of Appeals presents "serious legal questions" since it improperly construed the term "first sale" in the NGPA, results in the improper repeal by implication of FERC

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[10] No. 80-175-6-42T (W. Va. Dec. 10, 1981), *petition for cert. filed*, 50 U.S.L.W. 3768 (U.S. March 23, 1982) (No. 81-1672).

regulation of pipeline production under the Natural Gas Act, and failed to give proper deference to the contemporaneous interpretation of the NGPA by the FERC. Petitioners also contend that there may be a substantial economic impact resulting from the opinion below. Additionally, Michigan and AEPCO assert that *Mid-Louisiana* is in conflict with a decision of the highest court of a state. As shown below, the issues raised by Petitioners do not warrant review by this Court and, accordingly, the petitions should be denied.

A. *The Court Below Properly Interpreted the NGPA*

1. *The Court of Appeals Correctly Found that the Commission Regulations Under Review Failed to Recognize an Express Requirement of the NGPA*

The only issue now presented is an unexceptional question of statutory construction which does not warrant review by this Court. Applying recognized principles governing judicial review of an agency's interpretation of its statutory authority, the Fifth Circuit found that the comprehensive natural gas pricing program enacted by Congress in the NGPA did not authorize the FERC to continue cost-based regulation over natural gas production by a pipeline. Instead, in a clearly reasoned decision the court unanimously concluded that nothing in the language, purpose or history of the NGPA "suggests any intent to deny NGPA pricing to natural gas just because it is produced by a pipeline," and that "the unless clause of . . . [Section 2(21)(B)] can only have meaning if it is interpreted as granting 'first sale' status to gas which is attributable to pipeline production." App. at A-9.

The statute provides that sales of gas by a pipeline, distributor, or affiliate thereof, are not "first sales," and thus not subject to NGPA pricing, "*unless* such sale is attributable to volumes of natural gas produced" by such pipeline, distributor or affiliate thereof. 15 U.S.C. § 3301 (21)(B) (Supp. IV 1980) (emphasis supplied). The plain language of the "unless clause" shows the clear in-

tent of Congress that sales of gas *produced by* a pipeline, distributor or affiliate thereof are "first sales." (Sales by a pipeline or distributor of gas *purchased* by the pipeline, distributor or affiliate thereof are *not* first sales, because *that* gas was subject to a "first sale" when sold by the producer of the gas to the pipeline.) In this manner the NGPA provides that the price of all gas production is subject to the Title I pricing program. The court properly found that there simply would be no reason for Congress to include the "unless" clause if it did not intend that production by a pipeline, distributor or any affiliate thereof be accorded "first sales" status under the NGPA pricing scheme. App. at A-9.

The Commission regulations struck down by the Fifth Circuit allowed NGPA prices for production by affiliates of pipelines and distributors, but discriminatorily refused to allow such prices for production attributable to pipelines and distributors themselves. The FERC thereby attempted to amend the NGPA so as to continue cost-based regulation of pipeline production even though the plain language of that statute included production by a pipeline, and production by a pipeline affiliate, in the comprehensive national pricing program. Notably, not one of the Petitioners nor Amici advance a single basis for differentiating prior regulatory treatment of pipeline production from pipeline affiliate production, and neither the FERC nor any other party argues that the NGPA does not apply to sales of natural gas produced by pipeline affiliates. The court's decision simply recognized the clear applicability of the NGPA pricing program to all gas production, including pipeline and distributor production, and therefore vacated the conflicting FERC regulations.

2. *Congress Did Not Intend in the NGPA to Continue Cost-Based Regulation of Pipeline Production*

While the Fifth Circuit decision simply vacates FERC regulations that fail to implement the clear language and

purposes of the NGPA, Petitioners and Amici press their position by rearguing the policy decision already made by Congress, irrespective of the statutory language, purposes or history of the NGPA. In doing so, they suggest that the decision below abolishes regulation over the price of gas produced by pipelines and distribution companies. This is not correct. The only question is whether the *Congressional* pricing program is to be applied to all gas, or whether a special exception is to be created only for gas produced by pipelines and distributors. Clearly no such special exception is provided in the Act or was intended by Congress. Not only would such an exception be inconsistent with the purposes of the NGPA, but the legislative history of that statute will be searched in vain for any suggestion of such an exception. Neither Petitioners nor Amici cite to any such support.

The essential purpose of the NGPA was to establish a national pricing program applicable to the production of natural gas. Congress was fully aware of the prior cost-based manner of regulation, which had been applied to both independent producers and pipeline and pipeline affiliate producers, and clearly intended to supplant this manner of regulation as to all producers regardless of corporate organization. As disclosed by the Joint Explanatory Statement of the Committee on Conference accompanying passage of the NGPA, that Act was intended to establish a natural gas pricing policy which would apply to the first sale of "any" natural gas. H.R. Rep. No. 95-1752, 95th Cong., 2d Sess., *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983, 8991. No exceptions to this policy were set forth in the conference report or any place in the legislative history of the NGPA, and it is inconceivable that Congress would have carved out an exception to NGPA pricing for pipeline production without specifically addressing this exception. The Commission concedes that there is "no discussion of cost-of-service pricing in the statute or in its legislative history" (Pet. at 20), but then insists that Congress must have

intended the discriminatory treatment arising from the FERC's interpretation.

Other Petitioners also have failed to point to any legislative history indicating that Congress intended to exclude pipeline production from NGPA pricing and to continue FERC cost-based regulation of such production. On the contrary, the legislative history shows that the NGPA was intended to be a fundamental change in regulatory approach, as shown by the following explanation in the economic analysis accompanying that Act:

> [the NGPA] alters the present system of cost based controls on the wellhead price of natural gas sold in interstate commerce to a statutory price formula applicable to both interstate and intrastate sales. . . . It is apparent that the present dual market system of natural gas pricing, *including cost based regulation of the interstate market, is no longer tenable.*[11]

In this respect, Representative Dingell commented during House debate that the NGPA results in "the creation of a single, national market for natural gas *and an end to the economic distortions which accompanied the outdated mode of regulation under the Natural Gas Act.*" 124 Cong. Rec. 38,361 (1978) (emphasis supplied).

The clear purpose of Congress in the NGPA was to substitute Congressionally established prices for the previous cost-based system of natural gas pricing. As described in the Counterstatement of the Case, prior to the NGPA, cost-based pricing was applicable to independent, pipeline affiliate and pipeline production, although the specific cost-based methodology utilized may have varied from time to time. The FERC recognizes that there was no discussion of continuing cost-based regulation of pipe-

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[11] Staff of Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 2d Sess., Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978 (Comm. Print 95-62) (1978) (emphasis supplied).

line production in the Act or its history, but nonetheless claims that, while Congress intended to end cost-based regulation of independent and pipeline affiliate production, it did not intend to end cost-based regulation of pipeline production. The Act, however, does not distinguish between the corporate nature of the producer or the specific cost-based methodologies employed in arriving at a cost-based rate.[12]

It is apparent that the FERC regulations were an initial effort to continue what the FERC, not Congress, thought to be a desirable economic policy, *i.e.*, the continuation of cost-based regulation over pipeline production. However, the FERC's position was clearly rejected by Congress in passing the NGPA; the purpose of the NGPA was to drastically change all prior FERC cost-based pricing policies, by legislative action, and to create a unified national pricing plan for natural gas.

The statutory scheme reflected in the Court of Appeal's construction was expressly intended by Congress in passing the NGPA, as shown by the following considerations:

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[12] Petitioners attempt to justify the Commission's discriminatory treatment by implying that consumers have historically borne the costs and the risk of pipeline production but have not done so for independent producer or pipeline affiliate production (FERC Pet. at 15, Michigan Pet. at 5). This assumption becomes absurd when it is recognized that pipeline affiliate production was regulated under the NGA in exactly the same manner as pipeline production. ("Gas produced by an affiliate of a pipeline is treated for ratemaking purposes as if it were produced by the pipeline company itself." City of Chicago, *supra*, 458 F.2d at 737 n. 20.) Petitioners also ignore the fact that under prior area and nationwide rate regulation of independent, pipeline and pipeline affiliate producers alike, ratepayers also ultimately bore the costs of exploration and production. Indeed, in Opinion No. 699-H the Commission arrived at a national rate which included a provision for exploration and developments costs, including dry hole costs, and provided a sufficient return to cover the risks associated therewith. Just and Reasonable Rate for Sales of Natural Gas, 52 F.P.C. 1604, 1615-16 (1974), *aff'd sub nom.* Shell Oil Co. v. FPC, 520 F.2d 1061 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976).

1. Congress intended to, and did, remove the wellhead pricing of the *commodity*—gas—from the FERC and substituted a congressionally determined price structure. The Court of Appeals decision recognizes this fact.

2. The decision does *not* remove regulatory jurisdiction over rates for sales to the customers of the pipeline or distributor: that jurisdiction remains and has never been challenged. All the decision does is to require that the price of gas attributable to production by a pipeline or distributor is governed by the prices provided by Congress for all gas production, without discrimination.

3. It is not anomalous—as Petitioners claim—that 40 years of FERC jurisdiction over the price of gas produced by pipelines was ended by the NGPA, since ending FERC jurisdiction over the pricing of gas production was exactly what the NGPA was enacted to do. The NGPA also ended FERC cost-based jurisdiction over far larger amounts of gas produced by independent and affiliate producers in exactly the same way, reversing decades of prior practice there too (sales of gas produced by independent producers were held to be subject to federal regulation in 1954—24 years before passage of the NGPA). The opinion below does not "repeal by implication" the previous method of regulating pipeline production (New York Pet. at 11-12, Michigan Pet. at 14). Just as Congress displaced the prior NGA mode of cost-based regulation with respect to independent producers, Congress also specifically addressed the proper treatment of pipeline production in Section 2(21) of the NGPA and determined that the prior NGA mode of regulation would also be displaced with respect to pipeline production. The decision below recognizes this fundamental change in the pricing of natural gas production.[13]

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[13] A more dramatic change of regulatory pattern was accomplished by the NGPA, when it made the federal—Congressionally determined—price structure applicable to gas sold in *intrastate* commerce for the first time, which gas had never previously been subject to federal pricing controls.

4. It *would* be anomalous to read the NGPA—as Petitioners do—to eliminate FERC jurisdiction as to all gas *except* the relatively small volumes of pipeline and distributor production, and to discriminate against those volumes, not on the basis of whether they represent old or new gas, or deep or shallow gas, or high cost or low cost gas, but rather by *who produces* the gas. There is no suggestion in the statute or its purpose and history that such irrational discrimination was intended, and the Fifth Circuit avoided this result.

5. Petitioners agree that gas produced by affiliates of pipelines and distributors must receive NGPA prices. In light thereof, the refusal to allow the same prices for gas produced by the pipelines and distributors *themselves* would mean that pricing would depend upon the formality of what corporate form and ownership are used. The decision below avoids this senseless result.

6. The FERC asserts (Pet. at 20), that because independent producers do not always qualify for full NGPA prices where their contract prescribes a lower price, "[i]t would be anomalous to permit pipeline producers to qualify automatically for full NGPA prices by virtue of 'intracorporate transfers' that are not governed by contract or other indicia of a commercial transaction." In fact, the NGPA provides that the price for pipeline and pipeline affiliate "first sales" shall not exceed the amount paid in comparable "first sales" by non-affiliated producers, thereby precluding pipelines from "automatically" qualifying for full NGPA prices.[14] There would be no reason

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[14] Section 601(b)(1)(E), 15 U.S.C. § 3431(b)(1)(E) (Supp. IV 1980), provides:

> Affiliated entities limitation.—For purposes of paragraph (1), in the case of any first sale between any interstate pipeline and any affiliate of such pipeline, any amount paid in any first sale shall be deemed to be just and reasonable if, in addition to satisfying the requirements of such paragraph, such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.

for this limitation if Congress did not intend for production by pipelines or affiliates to be accorded NGPA pricing treatment, and the court's interpretation is fully in accord with this intent.

7. Finally, in contending that the decision below is incorrect because it fails to afford proper deference to the contemporaneous interpretation of the NGPA by the Commission, (New York Pet. at 11, FERC Pet. at 24), Petitioners disregard the fact that the courts are the final authorities on issues of statutory construction, and that an administrative interpretation is properly reversed where it is inconsistent with statutory language or history or it frustrates the policy that Congress sought to implement. *See Federal Election Comm'n v. Democratic Senatorial Campaign Comm.*, 102 S. Ct. 38, 42 (1981); *FMC v. Seatrain Lines, Inc.*, 411 U.S. 726, 745-46 (1973); *FPC v. Tuscarora Indian Nation*, 362 U.S. 99 (1960). The decision below recognized the Commission's contemporaneous interpretation of the statute, but found that the weight of this factor is diminished since the FERC admitted it had no input into the development of the term "first sale." App. at A-7. The court correctly interpreted the term "first sale" in accord with the policy that Congress sought to implement, and properly applied principles of statutory interpretation in finding that deference to the agency construction was inappropriate where that interpretation challenges "the clear meaning of a statute as revealed by its language, purpose and history." *Id.*

3. *The NGPA Clearly Contemplates that Pipeline and Distribution Company Production Should be Subject to the NGPA Pricing Program Applicable to "First Sales"*

Petitioners claim as a basis for this Court granting certiorari that pipeline and distribution companies cannot make a "first sale" because they allegedly make no "sales" of the gas which they produce. This assertion is

clearly incorrect, since they do sell such gas, along with gas which they purchase, to their customers. Whether that actual "first sale" of their own production is regulated as the "first sale," or whether the point of "first sale" is treated as the point of intracorporate transfer from producing properties to transmission properties, as the Court of Appeals correctly found, makes no practical difference. In either case, there is a "first sale" and NGPA pricing is applied, with the same effect on rates. The "unless clause" of Section 2(21)(B) of the NGPA plainly shows that pipeline and distributor produced gas *is* intended to be the subject of a "first sale" just like sales by independent producers and pipeline or distributor affiliates. There is *no* suggestion in that language that only *some* of such gas production is the subject of a "first sale." Yet that is the interpretation Petitioners would urge.

The Commission states that the intracorporate transfer theory is a "novel regulatory doctrine" (Pet. at 14), implying that it stands regulation on its head, but then notes that it has the discretion pursuant to its rulemaking powers under Section 501 of the NGPA to impose this "novel" doctrine by treating the intracorporate transfer as a "first sale." (Pet. at 16). In fact, the FERC admits that it actually has applied this "novel" doctrine in Order No. 98 by imputing a sale and applying NGPA "first sale" prices, as a matter of discretion under the NGA, to pipeline production previously receiving area or nationwide treatment (Pet. at 18 n.12). It is certainly peculiar that Congress could not itself have intended an intracorporate transfer to be a "first sale," but would allow the Commission to implement this "novel" regulatory approach by its general rulemaking authority under the NGPA. This claim is particularly strange since historically the FERC in applying area and nationwide rates to pipeline and affiliate production, had placed a value on such production at the point of intracorporate transfer from the pipeline's producing division

to its transmission division. Contrary to the Petitioners' assertions, the Fifth Circuit did not impose any "novel" regulatory structure warranting review by this Court.

In fact, the FERC's rulemaking powers under Section 501(b) of the NGPA with respect to "first sales" are circumscribed by that section, which provides that "[e]xcept where otherwise expressly provided," the Commission may define accounting, technical, and trade terms used in the NGPA, but any such definition "shall be consistent with the definitions set forth in this chapter." 15 U.S.C. § 3411(b) (Supp. IV 1980). The definition of "first sale" *was* expressly provided for, and the Conference Report explained that the Commission may "establish rules applicable to intracorporate transactions under the first sale definition." H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 116, *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983, 9033. The Court of Appeals correctly found that "[t]his comment assumes that intracorporate transactions will fall *within* the first sale definition. The decision which Congress committed to the Commission's judgment was whether regulations were necessary to govern those transactions." App. at A-12, A-13 (emphasis supplied).[15] The Fifth Circuit's decision is consistent with the plain intent of Congress to find a "first sale" at the point of intracorporate transfer.

The court also properly found that other provisions of the statute indicate that Congress both intended to accord pipeline production "first sale" status and contemplated that the intracorporate transfer would be treated

[15] The FERC notes that the court thereby read the phrase "under the first sale definition" as qualifying "intracorporate transactions," but claims that the "more reasonable interpretation" is that the Commission "may establish rules 'under the first sale definition' applicable to intracorporate transactions." (Pet. at 23). This is a distinction without a difference since even the FERC's interpretation assumes that intracorporate transfers can indeed involve "first sales" and that, to the extent required, the Commission may establish regulations to this effect.

as a "first sale." Title II of the NGPA provides for incremental pricing of certain gas whereby interstate pipelines would pass through to certain industrial users the "first sale acquisition" costs reflecting the "price paid" for gas under Title I above a specified threshold level. With respect to interstate pipeline and affiliate production, Congress provided in Section 203(b)(2) that for "any natural gas produced by an interstate pipeline or any affiliate of such pipeline, the first sale acquisition costs of such natural gas shall be determined in accordance with rules prescribed by the Commission." 15 U.S.C. § 3343(b)(2) (Supp. IV 1980). The court explained that:

> By referring to the "first sale acquisition cost of such gas," in terms of "any gas produced by any interstate pipeline," Congress must have contemplated that any gas produced by a pipeline would be subject to a first sale. Moreover, the fact that Congress provided that the "first sale acquisition cost" of pipeline produced gas would, like the first sale price paid to independent producers, be passed along to the pipeline's ultimate customers suggests that both prices were to be treated in a similar manner. . . . The first sale thus appears to refer to the intracorporate transfer."

App. at A-11, A-12. The FERC admits that Congress in Section 203(b)(2) provided a "rule of intracorporate transfer" in Title II, but asserts that this concept does not apply "in the very different context of Title I," and that if Congress intended an intracorporate transfer to be a "first sale" there would be no need for the special pipeline production rule in Section 203(b)(2). (Pet. at 23). To the contrary, the court below recognized that while the general rule defines "first sale acquisition cost" as the *price paid* in a "first sale," the special rule "reflects Congress' awareness that technically an intracorporate transfer involves no price paid." App. at A-12. Moreover, since Title II requires the incremental pricing

of certain "first sales" of gas produced and all of such gas falls within an NGPA pricing category,[16] Congress must have assumed that there would be a Title I "first sale" price of pipeline produced gas which would then be incrementally priced in accordance with Title II. It is specious to contend, as the FERC does, that Congress included this special rule for only the insignificant amount of pipeline production which is not commingled with other gas and which would therefore qualify for NGPA prices under the FERC interpretation of "first sale."

Petitioners' claim that there is no "first sale" of most pipeline produced gas is not only incorrect but would also lead to absurd results. Their interpretation would result in the exclusion of most pipeline production from the NGPA pricing program and the continuation of cost-based regulation of this production, while cost-based regulation of independent producer and pipeline affiliate production would be eliminated. Congress cannot be presumed to have intended the discriminatory results of Petitioners' interpretation. Pipeline produced gas qualifying for NGPA incentive prices, such as stripper well gas under Section 108 or Devonian shale gas under Section 107, is no less entitled to such incentive prices than is like gas produced by others. Yet under the construction Petitioners urge, gas produced from the same fields, and in some instances from the same wells, would be subject to vastly different prices, based solely on whether the producer was a pipeline (no incentive NGPA pricing) or a pipeline affiliate or independent producer (both subject to incentive NGPA pricing). This irrational construction perverts the statute and is inconsistent with previous efforts to treat pipeline production on a parity with production by independent producers.

In sum, a rational reading of the NGPA compels the conclusion that Congress intended that pipeline produc-

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[16] *See* Sections 203(a)(1)-(8), 15 U.S.C. §§ 3343(a)(1)-(8) (Supp. IV 1980).

tion be subject to NGPA first sale prices at the point of intracorporate transfer to the transmission properties of the pipeline. In a carefully considered opinion the Court of Appeals has properly applied the Congressional intent, and Petitioners have not provided any reasonable justification for disturbing this decision.

B. *Assertions of the Economic Impact of the Court of Appeals Decision Do Not Warrant Review*

The widely varying claims of Petitioners and Amici respecting the economic impact of the Court of Appeals decision do not present an important federal question justifying extraordinary review by the Court. Although the gas produced by pipelines and distributors constitutes a substantial volume, that volume, and its value, is but a small fraction of the total volume of gas produced for sale in the United States. Since all parties acknowledge that the NGPA changed the pricing system applicable to the more than ninety percent of total gas production attributable to independent producers or affiliates of pipelines and distributors, the question is simply whether Congress intended those same changes to apply to the remaining less than ten percent attributable to pipeline and distributor production. In addition, FERC Order No. 98, which was also vacated by the decision below, would have allowed NGPA pricing for a portion of pipeline produced gas in any event, thereby further reducing the practical impact of the court's decision.

The essential consideration is that Congress was aware of the economic impact of the NGPA—it balanced the equities and determined that a national pricing structure was required for all production of natural gas sold in the United States, regardless of the corporate form of the producing entity and regardless of whether the gas is sold in intrastate or interstate markets. Claims of "windfall profits" resulting from the opinion below (New York Pet. at 20, FERC Pet. at 15) were raised relative to all

producers when the NGPA was before Congress; Congress nevertheless took control from the FERC and set a uniform pricing policy for all gas produced in the U.S. Petitioners now simply are trying to reargue the issues, relative to pipeline producers, that Congress decided in enacting the NGPA. Petitioners' remedy is with the Congress and not with this Court.

C. *There is No Reason to Presume a Conflict Between the* Mid-Louisiana *and* Pennzoil *Decisions When a Conflict Is not Apparent*

Certain Petitioners have alleged a conflict between the decision of the Court of Appeals here and the decision of the West Virginia Supreme Court of Appeals in *Pennzoil Co. v. Public Serv. Comm'n of West Virginia*, *supra*, note 10. (AEPCO Pet. at 13, Michigan Pet. at 9-10).[17] This allegation is without merit.

It is not apparent that the West Virginia Supreme Court in its one page order in *Pennzoil* relied upon any definition of "first sale" in affirming the West Virginia regulatory Commission, since that Commission set forth several grounds for its decision and the court summarily denied Pennzoil's petition for review of the Commission decision without specifying the grounds.[18] The court simply did not reveal the basis for affirming the West Virginia Commission, nor any basis for presuming a direct or other conflict with the decision in *Mid-Louisiana*. In fact, the Public Service Commission of West Virginia,

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[17] The opinion of the West Virginia court is reproduced in Appendix A to Pennzoil Company's petition for certiorari at 1a.

[18] The other grounds relied upon by the Commission included claims that (1) Section 602 of the NGPA allows a state commission to fix intrastate rates, (2) state law allows any ratemaking method to be used, and (3) Pennzoil had failed to exhaust administrative remedies. *See* "Brief of the Public Service Commission of West Virginia in Opposition to Petition" at 8, Pennzoil Co. v. Public Serv. Comm'n of West Virginia, No. 81-1672 (filed April 9, 1982).

an Amici here, has advised this Court that in its view the "West Virginia Supreme Court of Appeals did not adopt as the basis for its decision the order of the . . . [FERC] which was reversed and vacated by the 5th Circuit in *Mid-Louisiana*," and further noted that it "views the *Pennzoil* case as involving separate legal grounds" from the decision in *Mid-Louisiana*.[19]

Clearly, there is no reason for this Court to find a conflict when a conflict is not apparent and there are independent reasons that the West Virginia court could have relied upon which would not result in a conflict with the Fifth Circuit. In any event, if the *Pennzoil* decision can be sustained on an independent or alternative ground, the fact that it conflicts with another appellate court does not constitute an adequate reason for the grant of certiorari. *The Monrosa v. Carbon Black, Inc.*, 359 U.S. 180 (1959). Even if it were assumed, *arguendo*, that the West Virginia court relied upon the interpretation of "first sale" in the FERC regulations that the Fifth Circuit vacated, that court might well reach a different conclusion if review of the Fifth Circuit decision is denied and the *Pennzoil* case is remanded. In sum, *Pennzoil* does not provide a basis for certiorari in *Mid-Louisiana*.

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[19] *See* "Response of the Public Service Commission of West Virginia to the Motion of Arizona Electric Power Cooperative, Inc., for Contemporaneous Consideration and Disposition of Petitions for Certiorari" at 2, Arizona Electric Power Cooperative v. Mid-Louisiana Gas Co., No. 81-1958 (filed April 29, 1982). The FERC also has admitted that "there is a substantial question in . . . [Pennzoil] whether the judgment of the West Virginia court rests on an independent and adequate state ground." "Memorandum for the United States and the Federal Energy Regulatory Commission as Amici Curiae" at 5, Pennzoil Co. v. Public Serv. Comm'n of West Virginia, No. 81-1672 (filed July 28, 1982).

CONCLUSION

The petitions raise no question warranting review by this Court of the opinion of the Court of Appeals below. Accordingly, the petitions should be denied.

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Petitioner's Reply Brief

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IN THE

Supreme Court of the United States

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v.

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Respondents.

On Petitions For A Writ Of Certiorari To The United States Court of Appeals For The Fifth Circuit

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REPLY OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK TO OPPOSITIONS TO PETITIONS FOR CERTIORARI

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TABLE OF AUTHORITIES

CASES: **PAGE**

Columbia Gas Development Corp. v. *FERC*, 651 F.2d 1146 (5th Cir. 1981) 5

Miller v. *Youakim*, 440 U.S. 125 (1979) 5

Red Lion Broadcasting Co. v. *FCC*, 395 U.S. 367 (1969) 5

STATUTES:

Natural Gas Policy Act, 15 U.S.C. §§3301 *et seq.*:

Section 2(21), 15 U.S.C. §3311(21) 5, 6, 7
Section 104, 15 U.S.C. §3314 2
Section 106(a), 15 U.S.C. §3316(a) 2
Section 108, 15 U.S.C. §3318 2
Section 501, 15 U.S.C. §3411 4
Section 601(b)(1)(E), 15 U.S.C. §3431 (b)(1)(E) 6

MISCELLANEOUS:

123 Cong. Rec. 29, 791 (1977) 2
123 Cong. Rec. 30,186 (1977) 6

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REPLY OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK TO OPPOSITIONS TO PETITIONS FOR CERTIORARI

The Public Service Commission of the State of New York (New York), petitioner in Case No. 81-1889, herewith files its reply to the various oppositions to the petitions for certiorari filed by New York, the Arizona Electric Power Cooperative, Inc., the State of Michigan and the Solicitor General on behalf of the Federal Energy Regulatory Commission (FERC or Commission) from the opinion of the Fifth Circuit Court of Appeals in *Mid Louisiana* v. *FERC*, 664 F.2d 530 (5th Cir. 1981).

The briefs in opposition which have been filed by seven of the major pipeline beneficiaries of the opinion

below are, in New York's opinion, of principal significance for what they do not, and cannot say. Thus:

1. The briefs in opposition do not dispute that the pipeline gas, which received cost-of-service treatment under the Natural Gas Act and would continue to receive such treatment under Commission Order Nos. 58 and 98 vacated by the opinion below, is flowing gas - in major part from wells commenced prior to 1973 on leases acquired prior to October 1969 - as to which the pipelines never assumed any risk since, under the Commission's cost-of-service pricing, they are reimbursed for all prudent costs regardless of the success of their efforts. This is, and has always been, in contrast with the pricing of gas for independent producers (and for pipeline produced gas which was, and remains eligible for the rates available to independent producers) where revenues are dependent upon the development and sale of gas.[1]

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[1]The suggestion at page 20, n. 18 of the brief in opposition filed by El Paso Natural Gas Company that petitioners have not suggested why the "stripper well" price of Section 108 of the NGPA should not apply to pipelines as well as independent producers is a good example of the pipelines' efforts to sweep this vital distinction under the rug. The high rate made applicable by the Congress to existing wells producing a maximum of 60 Mcf per day was intended as an incentive for the adoption of costly secondary and tertiary enhanced gas recovery techniques to wells which would otherwise be uneconomic to produce. (See comments of Senator Ford on Amendment No. 881, 123 Cong. Rec. 29,791 (1977)). While such an incentive might be required by an independent producer whose existing wells would otherwise command a much lower unit price pursuant to Sections 104 or 106(a) of the Act, it is not necessary for pipeline production priced on a cost-of-service basis since the pipeline, unlike the independent producer, would in any event be entitled to recover the full costs of such additional production efforts.

2. The briefs in opposition do not dispute that the additional revenues will be true windfalls to the pipelines involved, in that they are already securing all of their costs for the gas plus a reasonable return on their investment, and will not have to make any additional expenditures to secure the higher new prices. Nor can they claim that the additional price is necessary to induce either further redevelopment of the wells in issue - since the actual cost of such redevelopment would be recouped under cost-of-service pricing - or the development of new pipeline production, which will in any event secure NGPA ceiling rates under the Commission's orders.

3. While the briefs in opposition attempt in various ways to denigrate the significance of the additional costs the opinion below would impose upon gas consumers, they do not and cannot dispute petitioners' contentions that these costs will be in the hundreds of millions of dollars for a substantial number of years.[2] The possibility

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[2]The pipelines' briefs in opposition carefully refrain from specifying the increased revenues they claim under the opinion below. However, filings by various pipelines at the Commission indicate that New York may have underestimated the potential adverse impact on gas consumers in its petition. Thus, we had estimated at p. 19 of our petition that the annual impact of Columbia Gas Transmission Corporation repricing its cost-of-service production at NGPA rates would be about $38,400,000. However, Columbia's recent PGA filing of July 30, 1982 in FERC Docket No. TA82-2-21 projects old gas production of 18,127,900 Mcf for the six months ending February 28, 1983 at a cost under NGPA pricing of $73,175,323 for an average rate of $4.0366 per Mcf. The annualized cost for such gas of $146,350,646 compares with the 1981 cost of $20,247,093 for the same category of gas priced on a cost-of-service basis, as set out in Columbia's May 7, 1982 filing FERC Docket No. RP82-88. In short, the annual impact of the decision below for this one pipeline alone (without considering its claims for retroactive relief for the period December 1, 1978

that the aggregate annual increases in the cost of gas purchased by the nation's interstate pipelines from other sources will exceed the aggregate impact of the decision below does not minimize its significance especially when it is recognized that the gas presently subject to cost-of-service treatment under the Commission's orders, but authorized to secure much higher rates under the decision below, makes up a substantial percentage of the gas costs of the affected pipelines.[3]

4. The opposing briefs do not and cannot support the lower court's views as to why it was not required in the present case to give any significant deference to the Commission's views as to the meaning of the NGPA, in view of fact that the Commission is delegated the authority by Section 501 of the Natural Gas Policy Act, 15 U.S.C. §3411, to administer the Act, prescribe rules to implement its operation and define "accounting, technical and trade terms" used in the Act.

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through December 31, 1981) is approximately $125,000,000.

When it is recognized that Consolidated Supply Corporation, another pipeline serving New York, has stated in its PGA filing in FERC Docket No. TA82-2-22 that the decision below would increase its annual revenues by more than $27,000,000 annually, to which it has added a claim for retroactive relief of $115,339,429, it becomes apparent that the statement at p. 15, n. 11 of the Commission's Petition for Certiorari that the total increase in natural gas costs stemming from affirmance of the opinion below "will exceed $100,000,000 annually for the next several years" is extraordinarily conservative.

[3]Thus in the case of the respondent Mid-Louisiana Gas Company, old flowing gas now regulated on a cost-of-service basis accounts for approximately 3,800,000 Mcf out of total annual sales of 35,571,600 Mcf, or 11% of the pipeline's gas supply. See Mid-Louisiana's filing of June 1, 1982 in FERC Docket No. TA82-2-15, Exhibit A. The total cost of this gas at NGPA rates is approximately $10,970,000 as contrasted with a cost-of-service cost of approximately $675,000.

The court of appeals recognized that in prior cases involving the interpretation of the NGPA it had given great deference to the Commission's views. See, e.g., *Columbia Gas Development Corp.* v. *FERC*, 651 F.2d 1146, 1155 (5th Cir. 1981). It concluded that such deference was not required here because the Commission's interpretation, though a contemporaneous one by the agency established by Congress to administer and interpret the Act, did not have the sanction of long years of acceptance and, in the court's view "does not concern an area particularly within the agency's expertise" since the Commission did not actively participate in the drafting of the language of Section 2(21) of the Act. This ignores the fact that the Commission was intimately familiar with the differences between its regulations of pipeline produced gas, and gas produced by independent producers. The Commission's interpretation of Section 2(21) was, of course, not sacrosanct. But the court below could not substitute its own interpretation unless there were "compelling indications that it was wrong." See *Red Lion Broadcasting Co.* v. *FCC*, 395 U.S. 367, 381 (1969); *Miller* v. *Youakim*, 440 U.S. 125, 144, n. 25 (1979). As demonstrated in New York's petition, the court's showing does not approach this level.

5. The opposing briefs do not and cannot deny that throughout the lengthy consideration of the various proposals that resulted in the adoption of the NGPA, there was no suggestion by the piplines or any other person or group that the Commission's regulation of pipeline production under the Natural Gas Act was inhibiting optimum production or otherwise acting in a manner contrary to the public interest. Instead they focus upon Congress' expressed dissatisfaction with the Natural Gas Act regulation of the per Mcf rates at which

producers were authorized to sell gas to the pipelines. Nor do the opposing briefs point to a single statement in the Congressional reports or debates indicative of an intent to change the existing mode of regulation of pipline production.[4] Since the language of Section 2(21) is consistent with the maintenance of the *status quo* with respect to regulation of pipeline production, this lack of any indication of a contrary intent necessarily takes on significance.[5]

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[4]While there are no statements in the legislative history directed to pipeline production, the bill that passed the Senate would have deregulated all new gas "sold *or delivered* in interstate commerce for the first time after January 1, 1977," and in Section 5 of the bill limited the automatic passthrough of costs where a pipeline "purchases new natural gas from an affiliate *or produces new natural gas from its own properties*" to situations where the rates or charges for such gas did not exceed those for comparable sales between persons not affiliated with the pipeline. See 123 Cong. Rec. 30,186 (1977). However, the NGPA as enacted applied only to "first sales" and the passthrough language of the Senate bill was amended to delete from the analogous Section 601(b)(1)(E) all references to gas produced from a pipeline's own properties.

Thus, as indicated in New York's petition, and contrary to several of the briefs in opposition, the language of Section 601(b)(1)(E) supports the Commission's interpretation of the scope of "first sales" rather than that of the court of appeals.

[5]The court below attempts to overcome this deficiency in its approach to the problem by suggesting that "nothing in the language used here or elsewhere in the NGPA suggests any intent to *deny* NGPA pricing to natural gas just because it is produced by a pipeline." (Pet. App. A8-A9, emphasis added.) But repeal of existing statutory authority by implication is not the rule and the failure of Congress to deny this was its intent is clearly not a basis for concluding it must have intended to do so.

6. The opposing briefs fail to support the statement of the court below that the transfer of gas between the pipeline's production and transmission "division" must be characterized as a first sale, with the consequence that *all* pipeline production will be eligible for NGPA ceiling rates, because under the Commission's construction all natural gas produced by a pipeline allegedly "would be denied 'first sale' status under NGPA" (Pet. App. A-8). If an either/or result was required by the language of the Act, New York would argue, for the reasons detailed in our petition, that the Commission's reading was still correct. In fact, however, it is the court of appeal's construction, alone, which produces such an absolute result.

The Commission's construction, consistent with the Congressional indications that first sales are "wellhead sales,"[6] treats pipeline production sold in the field to

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[6]Title I of the NGPA which establishes ceiling prices for various categories of first sales is entitled "Wellhead Pricing" with Subtitle A entitled "Wellhead Price Controls." The court of appeals rejected Commission reliance on this language because Order No. 58 had recognized that some sales by producers could qualify as first sales despite the fact that they were made downstream of the well, i.e., at the tailgate of a producer-owned gas extraction plant. (See Pet. App. A-10). But these sales, unlike the situation with pipeline production which without any contract or transfer for value become a fungible portion of the pipeline's total gas supply, are functionally the same as wellhead sales in that they are actual sales of gas attributable solely to the selling producer.

other pipelines, distributors or end users like the equivalent sales by producers, while, maintaining the distinction between such sales and pipeline production which is never the subject of any sales contract and for which a just and reasonable unit price had never had fixed by the Commission.[7] The fact that only a relatively small percentage of pipeline production has ever been "sold" — except as part of a mixture with gas purchased from independent producers *expressly* excluded from the first sale definition, does not vitiate the logic of the Commission's analysis.

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[7]The briefs in opposition do not dispute New York's contention that the transfer of gas between the production and transmission departments of a pipeline is neither a "sale", nor "transfer for value" as those terms are interpreted in contract law. Instead, like the court below, they rely on language in the Conference report on the NGPA authorizing the Commission "to define terms such as 'transfer for value' used in the definition of first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition." New York disagrees with the Commission's view (Pet. App. B-65) that this language gives it the discretion "to impute a sale at the wellhead and thereby accord first sale treatment to pipeline production" where no sales exist as a matter of law. However, even assuming that language in a Congressional report on a bill could give it such authority, it is apparent that the language did not mandate such action. Thus, unless the language of Section 2(21) mandated a different result - and neither the court below nor any brief opposing certiorari argues that it does - the Commission as a matter of policy could adhere to the normal contract law and reach the conclusion it did.

CONCLUSION

For the reasons set forth above and in New York's original petition it is clear that the present case presents a novel question of statutory construction of great and continuing significance to the administration of the key new legislation affecting the regulation and operation of the natural gas industry. It is also manifest that the court of appeal's determination, substituting its interpretation of the application of the term "first sale" to pipeline production for that of the agency entrusted with the authority to administer and interpret the Act, raises serious questions of legislative interpretation and the role of reviewing courts. Under these circumstances the petitions for review filed by New York and other parties, including the Commission, should be granted.

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September 20, 1982

Amicus Brief

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Respondent.

On a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE ON BEHALF OF ASSOCIATED GAS DISTRIBUTORS AND BRIEF AMICUS CURIAE

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May 11, 1982

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ASSOCIATED GAS DISTRIBUTORS

Member Companies

Baltimore Gas and Electric Co.
Bay State Gas Co.
The Berkshire Gas Co.
Boston Gas Co.
The Brooklyn Union Gas Co.
Cape Cod Gas Co.
Chesapeake Utilities Corp.
City of Holyoke, Mass., Gas and Electric Dept.
City of Westfield Gas and Electric Light Dept.
Commonwealth Gas Co.
Concord Natural Gas Corp.
The Connecticut Gas Co.
Consolidated Edison Company of New York, Inc.
Delmarva Power and Light Co.
Elizabethtown Gas Co.
Fall River Gas Co.
Fitchburg Gas and Electric Light Co.
Gas Service, Inc.
Haverhill Gas Co.
Long Island Lighting Co.
Lowell Gas Co.
Lynchburg Gas Co.
Manchester Gas Co.
New Jersey Natural Gas Co.
New York State Electric and Gas Corp.
Northern Utilities, Inc.
Pequot Gas Co.
Philadelphia Electric Co.
Philadelphia Gas Works
Providence Gas Co.
Public Service Company of North Carolina, Inc.
Public Service Electric and Gas Co.
South County Gas Co.
South Jersey Gas Co.
The Southern Connecticut Gas Co.
Tiverton Gas Co.
UGI Corporation
Valley Gas Co.
Washington Gas Light Co.

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MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

Associated Gas Distributors (AGD)[1] hereby respectfully moves pursuant to Rule 42(3) for leave to file the attached brief as *amicus curiae* in this case. The consent of counsel for the petitioner has been obtained, but counsel for respondents have objected.

[1] The AGD member companies are listed on the inside cover of this motion and brief.

I.

STATEMENT OF INTEREST

Associated Gas Distributors is an unincorporated association of gas distribution companies serving over 11 million customers along the Eastern Seaboard or approximately twenty-five percent of the nation's interstate natural gas customers. AGD member companies rely almost exclusively on interstate pipeline companies for their gas supplies. Since the principal pipelines supplying gas to the east coast have been paying maximum lawful ceiling prices under the Natural Gas Policy Act of 1978 (NGPA), AGD member companies have experienced dramatic price rises and find it increasingly difficult to provide adequate and reliable service at just and reasonable rates to their customers.

Because the AGD member companies depend heavily on gas supplies available to the interstate market, they are deeply concerned that the decision of the Court of Appeals will result in a further escalation of prices when the NGPA pricing mechanism is applied to intracorporate transfers of production from pipeline affiliates. AGD member companies may be adversely and directly affected by the outcome of the present case.

II.

REASONS FOR GRANTING THE MOTION

The decision of the Court of Appeals held that, notwithstanding the explicit terms of Order No. 58 of the Federal Energy Regulatory Commission (FERC) excluding intracorporate transfers from the scope of "first sales" within the meaning of Section 2(21) of the NGPA, such intracorporate transfers were legally entitled to "first sale" treatment and, therefore, eligible for the higher NGPA prices.

The statutory interpretation adopted by the Court of Appeals and the vacating of Orders No. 58 and 98, if

affirmed, will have serious and far reaching implications for the pricing stability of interstate gas supplies. Since December, 1978, the price of gas acquired by interstate pipelines from their non-affiliated producer-suppliers has risen dramatically (by more than 100 percent) as a result of the NGPA. The prices applicable to gas acquired by pipelines from their own production sources is now all the more crucial to adequate interstate service. Yet, the decision of the Court of Appeals would abandon the lower, cost-of-service[2] pricing of significant volumes of pipeline-owned affiliate production and permit prices for such gas to rise without the restraint of FERC regulatory authority under the Natural Gas Act.

The petitioner has consented to AGD's filing of a brief *amicus curiae*. At this time, it is not clear what position, if any, the Commission will take in this Court.[3] No other party may be expected to advance generally the interests of natural gas distribution companies nor specifically represent the East Coast companies that will be significantly affected by generally higher NGPA prices for affiliate production sold in the interstate market.

The Court must look beyond the narrow definitional question, as stated by the Court of Appeals, to the fundamental issue of the role of the Commission under the NGPA to protect the consumer from prices no higher than necessary to assure adequate supplies, *i.e.*, to protect the stability of present and future interstate natural gas prices. As the representative of companies selling

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[2] Under this method pipelines recover from their customers all operating expenses, depreciation, taxes and a fair return on investment—including exploration, development and production costs. Rates are determined by dividing total costs by the volume of gas produced.

[3] *See* Application for an Extension of Time to Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit, filed by the Solicitor General herein, page 2.

gas to a large portion of the nation's consumers, AGD has a unique perspective on this issue which should be valuable to the Court's deliberations.

III.

CONCLUSION

Accordingly, and for the reasons stated above, Associated Gas Distributors respectfully urges the Court to grant this motion so that AGD may present its views in the attached brief.

Respectfully submitted,

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INDEX

	Page
Table of Authorities	iv
Interest of Amicus Curiae	1
ARGUMENT	5
I. The Decision of the Court of Appeals Imposing the NGPA "First Sale" Structure on Intracorporate Transfers Fails to Satisfy the Statutory Threshold Requirement for a "Sale"	5
II. The Decision of the Court of Appeals Will Have Significant, Adverse Economic Consequences for Interstate Gas Consumers Beyond the Particular Facts of This Case	6
CONCLUSION	16

TABLE OF AUTHORITIES

CASES — Page

Atlantic Refining Co. v. *Public Service Comm'n of New York*, 360 U.S. 378 (1959) 8, 14, 16

Columbia Gas Development Corp. v. *FERC*, 651 F.2d 1146 (5th Cir. 1981) 15

Federal Power Comm'n v. *Hope Natural Gas Co.*, 310 U.S. 591 (1944) 9

Federal Power Comm'n v. *Natural Gas Pipeline Co.*, 315 U.S. 575 (1942) 14

Federal Power Comm'n v. *Transcontinental Gas Pipeline Corp.*, 365 U.S. 1 (1961) 9

Mid-Louisiana Gas Co., et al. v. *FERC*, 664 F.2d 530 (5th Cir. 1981) 5

Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 10, 14, 15

Penzzoil Co. v. *Public Service Comm'n of W. Virginia*, No. 80-175-G, 42T (unreported opinion of the Supreme Court of W. Virginia) *cert. pending*, No. 81-1672 (filed March 10, 1982) 15

Sunray Mid-Continent Oil Co. v. *FPC*, 364 U.S. 137 (1960) 9

United Gas Improvement Co. v. *Callery Properties*, 382 U.S. 223 (1965) 14

REGULATIONS AND ORDERS OF THE FEDERAL ENERGY REGULATORY COMMISSION

18 C.F.R. 2.56(a)(g) and (b)(h) 10

18 C.F.R. 2.75 10

18 C.F.R. 2.76 10

Order No. 58, Docket No. RM 80-7 (Issued November 14, 1979) ..... *passim*

Order No. 93A, Docket No. 80-33 (Issued April 24, 1981) 16

Order No. 98, Docket No. RM 80-6 (Issued August 4, 1980) ..... *passim*

Order No. —, Docket No. TA 82-2-23 (Filed March 1, 1982) 3

TABLE OF AUTHORITIES—Continued

STATUTES — Page

Department of Energy Act, 91 Stat. 565, 42 U.S.C. §§ 7171, *et seq.* 6
Natural Gas Act, 52 Stat. 821, *as amended*, 15 U.S.C. §§ 717, *et seq.* ..... *passim*
Natural Gas Policy Act of 1978, 92 Stat. 3352, 15 U.S.C. §§ 3301, *et seq.* ..... *passim*

MISCELLANEOUS

U.S. Department of Energy, *Gas Supplies of Interstate Natural Gas Pipeline Companies—1980* (December, 1981) 7

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1889

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondent.

On a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF AMICUS CURIAE ON BEHALF OF ASSOCIATED GAS DISTRIBUTORS IN SUPPORT OF PETITIONERS

INTEREST OF AMICUS CURIAE

Associated Gas Distributors (AGD) is an unincorporated association of gas distribution companies serving over 11 million customers along the eastern seaboard, or approximately 25 percent of the nation's interstate nat-

ural gas customers. Virtually all of the gas purchased and resold by AGD member companies is acquired from the major interstate pipelines. These pipelines' production sources include significant volumes of gas transferred from their own production divisions to their transportation divisions by intracorporate transfers. Thus, AGD will be directly subjected to the generally higher prices which will result from the decision of the Court of Appeals to treat all such intracorporate transfers as "first sales" under the Natural Gas Policy Act (NGPA).

The Federal Energy Regulatory Commission (FERC or the Commission) has permitted the interstate pipelines to recoup their natural gas "first sale acquisition cost" from customers through the "pass-through" provisions of Title VI of the NGPA. The dollar impact of the court's decision depends on the difference between the current cost-of-service prices for production of gas from a pipeline's own sources and the NGPA prices for certain categories of gas—which now ranges from $.55 to $3.33 per thousand cubic feet (Mcf)—multiplied by the productive life of the established reserves. Increased costs for "first sale" gas will force AGD members to raise the rates to their consumers to recover this added expense.

As public utilities, AGD member companies are legally obligated to protect the interests of their customers. The immediate consequences of repricing old gas pursuant to the decision of the Court of Appeals is directly contrary to such interests because it adds significantly to the economic burdens of gas consumers without any commensurate supply benefits.

Further, the higher pipeline rates resulting from the Fifth Circuit's decision are directly contrary to the interests of the AGD member companies themselves. The increased retail rates resulting from this decision will

impair the competitive position of gas in the fuels marketplace. Competitive considerations are especially important in large volume industrial fuel markets since many industrial users have the capacity to switch from gas to alternate fuel sources, depending on the comparative retail price of such fuels.

The Fifth Circuit's decision to vacate Orders No. 58 and 98 exposes AGD members and their customers to substantial cost increases whose magnitude may rise dramatically if applied retroactively to the December 1, 1978 effective date of the NGPA.

Indeed, several pipelines are now relying on the decision below to justify requests for increased purchased gas adjustments (PGA) not only for future intracorporate transfers but for transactions dating back to December 1, 1978. They argue that the Court of Appeals decision means that all pipeline production was subject to NGPA prices from the time of its effectiveness. For example, in a recent rate filing by El Paso Natural Gas Company (El Paso), FERC Docket No. TA 82-2-33, the company claimed that implementation of that decision would increase its "purchased gas costs" by 39.15 cents per Mcf or $259 million for the six month period ending September 30, 1982. In addition, El Paso claimed that retroactive implementation of *Mid-Louisiana* for the period December 1, 1978 through December 31, 1981 would increase its purchased gas costs by a net additional $109 million.[1] Thus, the excess of NGPA prices over the cost-of-service rates for just one pipeline is at least $368 million for a 46 month period.

It is clear, however, that the Court of Appeals did not address the issue of retroactivity. If this Court should affirm the decision below, the case should be remanded, nonetheless, to the FERC to make the factual determina-

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[1] FERC Docket TA 82-2-23, filed March 1, 1982.

tion on a case-by-case basis as to the propriety of a retroactive application.

If the FERC were to approve a request for retroactive application of the ruling below, thereby allowing pipelines to impose a surcharge to recover for "undercollections" in past periods, two serious consequences would result. First, an unfair burden would be imposed on those gas consumers in the system at the time of the surcharge, while a benefit would be conferred on those gas customers who received gas at lower, cost-of-service pricing from 1978 to 1981. Second, such a surcharge would have a disruptive impact on the natural gas market by introducing an element of temporary volatility in retail rates which would confuse rational choices regarding energy uses. No useful purpose would be served by these retroactive payments of higher rates. Such payments do not inspire investments in future gas exploration projects nor are they required to compensate gas sellers for their efforts (this purpose is met by the cost-of-service ratemaking adopted by FERC in Orders No. 58 and 98).[2]

Since AGD member companies depend almost exclusively on gas supplies available to the interstate market, they are concerned that the decision of the Court of Appeals will force the upward repricing of flowing gas without any rational basis in federal gas pricing policy. These companies are especially concerned that one court has unilaterally interpreted the NGPA to repeal all vestiges of the consumer protection role originally delegated to the Commission by Congress.

Accordingly, AGD has a substantial and direct interest in this case, will be adversely and directly affected if the decision of the Court of Appeals is upheld and submits the present amicus brief in support of petitioners.

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[2] Order No. 58, Docket No. RM 80-7 (issued November 14, 1979, and Order No. 98, Docket No. RM 80-6 (issued August 4, 1980), reprinted at App. B.

ARGUMENT

I. The Decision of the Court of Appeals Imposing the NGPA "First Sale" Structure on Intracorporate Transfers Fails to Satisfy the Statutory Theshold Requirement of a "Sale."

This is a case of first impression, involving legislation critical to maintaining a stable, national energy policy. In reaching the decision to reverse the statutory interpretation of the Federal Energy Regulatory Commission and to vacate two of its orders, the Court of Appeals held that intracorporate transfers, from the production division to the transportation division of the same natural gas pipeline company, constituted a "first sale" within the meaning of the Natural Gas Policy Act (NGPA). The Court of Appeals reversed the determination of the Commission—the agency authorized to administer and interpret the NGPA—and concluded that intracorporate transfers constituted a "first sale" within the meaning of the NGPA and that those volumes of gas were thus automatically entitled to the maximum ceiling prices of Title I of the NGPA.[3]

In its enthusiasm to express its own interpretation of the NGPA, the Court of Appeals failed, however, to take account of the need for such intracorporate transfers to satisfy the threshold definition for a "sale"—namely, a transfer for value—prior to bringing such transactions within the scope of a "*first* sale" (emphasis added), as defined in Section 2(21) of the NGPA. The absence of this indispensable statutory prerequisite creates a fatal, substantive flaw in the decision below. This issue is clearly presented at pages 10-17 of the Petition for a Writ of Certiorari filed by the Public Service Commission of the State of New York and incorporated

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[3] *Mid-Louisiana Gas Co., et al.* v. *FERC*, 664 F.2d 530 (5th Cir. 1981), reprinted herein, Petitioners App. A-1. To avoid unnecessary duplication *amicus curiae* incorporates by reference Petitioners Appendices (App. —).

by reference herein to avoid unnecessary repetition of that analysis.

II. The Decision of the Court of Appeals Will Have Significant, Adverse Economic Consequences for Interstate Gas Consumers Beyond the Particular Facts of This Case.

1. *The Price, Supply and Consumer Protection Ramifications of the Fifth Circuit's Decision.*

This case presents the Court with an issue critical to the future of natural gas pricing policy and to the nation's gas consumers. Simply stated, the Court is challenged here to define what remains, if anything, of the historic role of the FERC[4] as a protector of the consumer's interest insofar as natural gas prices are concerned.

The decision of the Fifth Circuit creates the economic anomaly of substantially higher prices for gas from properties dedicated to the service of the public with no assurance or expectation that such prices will serve as an incentive to increase natural gas supplies. As a result of repricing gas from "old" pipeline-owned production sources, a classic economic windfall is conferred on those pipelines which happen to have large investments in older, still-productive acreage.

The size of this windfall is likely to be enormous, although precise measurement is impossible at this time. If the Fifth Circuit's approach is followed, intracorporate transfers of pipeline-produced gas may ultimately be found to qualify for "prices" equal to those available for non-affiliated sales under NGPA Sections 108 or 109. Gas on which the pipelines would be entitled to record a "book cost" of less than $1.00 per million Btu under

[4] The functions of the Federal Power Commission (FPC) were transferred to the Federal Energy Regulatory Commission (FERC) in 1977 by the Department of Energy Act, Pub. L. 95-91, August 4, 1977, 91 Stat. 565.

FERC Orders No. 58 and 98 would instead be repriced at either $2.18 or $3.33 per MMBtu under the Fifth Circuit's "first sale" theory.[5] Assuming a per-MMBtu increase of $1.00 were thus made applicable to *one-half* of the total volume of pipeline-owned production occurring in 1980, the aggregate windfall would be over $325 million for the year 1980.[6] The burden of this windfall is certain to endure for many years. The total volume of pipeline-owned gas reserves amounted to some 11 trillion cubic feet in 1980, a reserve base equal to about 10 percent of the total gas reserves in the U.S. These reserves, in the normal course, will probably be depleted over the next 10 to 20 years. Using the same $1.00 per MMBtu factor as the net increase in unit price available on pipeline-owned gas reserves, (and assuming only one-half of all pipeline production is affected), the long term value of the windfall derived from the "first sale" treatment of pipeline production is in the range of $5 to $6 billion.

The arbitrary action by the Fifth Circuit thus will burden consumers with an unfair pricing scheme from which they receive no benefit. The added revenues derived by pipelines from production of gas from pre-1973 wells cannot possibly operate as an incentive for

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[5] According to NGPA Title I, gas sold in May, 1982 under NGPA Section 108 is subject to a ceiling price of $3.335 per MMBtu; gas sold under NGPA Section 109 is subject to a ceiling price of $2.180 per MMBtu.

[6] According to Table 26 of *Gas Supplies of Interstate Natural Gas Pipeline Companies*, December, 1981, Energy Information Administration, U.S. Department of Energy, the major interstate pipelines acquired 651,018 million cubic feet of their 1980 gas supplies from company-owned reserves. An unknown fraction of this total was acquired on the "cost-of-service" basis prescribed by FERC Orders No. 58 and 98 and would be subject to "first sale" pricing under the decision below. As an industry norm, a cubic foot of natural gas contains 1000 Btu, *i.e.*, one Mcf (or thousand cubic feet) of gas is equivalent to one million Btu.

the drilling of new wells, sales from which are subject to other, higher NGPA ceiling prices unaffected by this case. The non-existence of any incentive function in the pricing system adopted by the court below is in direct contrast to the incentive pricing scheme adopted for gas producers under the Natural Gas Act of 1938 (NGA) and refined in the Natural Gas Policy Act of 1978.

Since December, 1978, the incentive rate scheme embodied in the NGPA has resulted in significant increases in natural gas prices. The NGPA authorized FERC to oversee the proper administration of the Act.[7] To retain order and stability in the natural gas marketplace, FERC moved quickly in Order No. 58, *supra*, to define the relationship between intracorporate transfers and "first sales" within the meaning of Section 2(21) of the Act. It properly exercised its discretionary authority in Order No. 98 to retain cost-of-service pricing for older pipeline affiliate production under its NGA pricing authority, while permitting gas produced by pipelines from post-1972 wells to receive the NGPA ceilings. FERC's exercise of authority in these Orders was consistent with industry practice over the past forty years and with the self-evident principle that prices applied to gas from wells long since discovered and committed cannot serve an *incentive* function.

This Court has long recognized that a fundamental purpose of the Natural Gas Act of 1938 was "to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges." *Atlantic Refining Co. v. Public Service Comm'n. of New York*, 360 U.S. 378, 388 (1959). In response to a need to protect the interest of the consumer in the pricing and supply of natural gas, Congress in 1938 imposed on the interstate pipelines an elaborate regulatory scheme. It is beyond cavil that the Federal Power Commission, the predecessor

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[7] 15 U.S.C. § 3411.

of FERC, was granted broad powers to police the gas marketplace in order "to protect consumers against exploitation at the hands of natural gas companies." *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 610 (1944). *See FPC v. Transcontinental Gas Pipeline Corp.*, 365 U.S. 1, 19 (1961); *Sunray Mid-Continent Oil Co. v. FPC*, 364 U.S. 137, 147 (1960).

When the NGPA was passed in 1978, its express purpose was to correct the inequities arising from the dual interstate and intrastate markets and to provide higher prices as an incentive to increased gas exploration and production. To meet these ends, the congressional blueprint established a scheme of higher maximum price ceilings for different categories of wellhead or "first" sales of natural gas and eligibility criteria for each category but included no specific directive insofar as the pricing of gas produced by regulated pipelines is concerned. The court below acknowledged these purposes and the absence of any express reference to the "first sale" definition in the legislative history of the Act. App. A-10. Yet, the court below ignored the incentive purpose of the NGPA price structure by giving meaning to this silence in the legislative history. *Id.* at 11-12. Nothing in the language, legislative history or contemporaneous interpretation by the Commission even remotely supports the conclusion that the NGPA's silence about the existing regulation of pipeline production under the Natural Gas Act and particularly the Commission's treatment of intracorporate transfers under existing regulatory policy were to be superseded or that the Commission's role in protecting the gas consumer from price exploitation had been abandoned. In second guessing the Commission, the Court of Appeals failed to recognize that nothing in the 1978 Act repeals the Commission's authority over pipeline production under the Natural Gas Act.

There is no justification in precedent for concluding that NGPA left the Commission without authority to

reaffirm its historical, cost-of-service approach to gas delivered from older pipeline production sources. Different pricing schemes for different kinds of production are not new. *See Permian Basin Area Rate Cases*, 390 U.S. 747, 795-797 (1968). This Court has sanctioned the broad authority of the Commission to develop pragmatic solutions for balancing the industry's and the consumers' interests in stable natural gas supply and price policies. Indeed, the Court has held that "the width of administrative authority must be measured in part by the purposes for which it was conferred . . . . Simply, the Commission's broad responsibilities therefore demand a generous construction of its statutory authority." *Id.* at 776. Two different ceiling rates were approved for gas produced from the Permian Basin area, deepnding on the "vintage" or age of the wells in question. In *Permian* the Court held "that price should be employed functionally, as a tool to encourage the production of appropriate supplies of natural gas." *Id.* at 796.

Here, the Commission followed a similar course. Orders No. 58 and 98 achieve a pricing system for pipeline-owned gas production which applies (a) the NGPA ceiling prices, i.e., the Congressionally-decreed *incentive* rate structure, in the case of gas produced from all post-1972 wells and (b) the traditional, cost-of-service pricing regulation in the case of gas produced from wells drilled in 1972 and earlier.[8] Although dismissed as "sophistic" by the court below, the Commission's bifurcation of the pricing system governing pipeline-owned production is a wholly rational adaptation of the NGPA incentive pricing structure. It *encourages* pipeline pro-

[8] It is important to note that, short of eligibility for the maximum prices under the NGPA, other regulatory procedures for increased rates are available to the pipelines if they, in fact, are not obtaining a sufficient return on their investments to continue production of the gas in question. *See, e.g.*, the special relief regulations under the Natural Gas Act, 18 C.F.R. 2.56(a)(g), 2.56(b)(h), 2.75, and 2.76.

duction activity (by extending NGPA incentive rates to pipeline-produced gas from newer wells) and wisely minimizes the size of the enormous and senseless windfall given to the pipelines under the approach taken by the court below. Given the pipelines' status as fully-regulated entities under both the Natural Gas Act and NGPA, such a pricing system was not an unreasonable exercise of agency discretion in a context where no Congressional mandate was provided.

2. ***Downstream Economic Consequences to Gas Distributors and Their Customers.***

Application of the decision of the Court of Appeals to the reality of the fuels market in 1982 and thereafter will cause economic dislocations in the fuels marketplace. Industrial demand *is* very sensitive to variations in price for fuels. Typically, major industrial customers construct facilities with alternate or dual fuel capability. Fuel choices are made on a day-to-day basis by large volume users with the capacity to switch from oil to gas and back again as price fluctuations occur.

By increasing the effective price of pipeline-produced natural gas, the decision below adds another significant increment to the current and future cost of gas sold at retail to price-sensitive industrial customers. The day is thus hastened, if not created, when those users abandon gas for other fuels, such as No. 6 fuel oil. With industrial users making fuel decisions on a day-to-day basis, it is incumbent on the Court to expedite review of this case to protect the natural gas distributors and their industrial customers from the unjust price increases which will arise from the decision of the court of appeals.

In this highly volatile market, higher prices for a pipeline's own production further exacerbate the competitive market circumstances of gas distributors *vis-a-vis* other fuel suppliers. This occurs at a time when

competitive retail price margins are slim, especially with regard to large, price sensitive industrial users. Current quotations show that the price of No. 6 fuel oil has been running marginally above the price of natural gas in recent months. This position could reverse itself instantly were the decision below to be implemented.

The "domino effect" of this policy would destabilize natural gas pricing policy and would further undermine the economic vitality of many distribution companies. Loss of distribution companies' industrial load would impose substantial additional costs on residential and small commercial gas users at a time when those users have already experienced some of the largest price increases in the history of the industry under the NGPA (on the average, monthly gas bills have doubled for residential consumers since 1978). An unnecessary price increase affecting the broad gas consuming public and resulting solely from judicial intervention in the pricing scheme fashioned by Congress and the Commission, should not be tolerated by this Court.

Finally, it should be clear that state and local governments are not in a financial position to absorb increased costs for fuel supplies when their local budgets are so vulnerable to spending cuts and to tax reductions—both of which leave no flexibility in a budget for a line item entitled "unforeseen fuel costs." Taxpayers are frustrated with greater demands on their local government budgets in the wake of federal program cutbacks. Of course, they must continue to perform public services, to heat public buildings, etc. At some point, local and state governments can be expected to encounter serious hardships with higher gas prices and to resort to alternative fuels or simply to close facilities.

Increases in natural gas prices which, as here, do not operate as an incentive for greater gas supplies, serve none of the goals of either the Natural Gas Act or the

Natural Gas Policy Act. The sponsors of the NGA legislation, in testimony and in floor speeches and reports, left no doubt as to their intent that the bill was consumer legislation. The NGPA did nothing to undermine the NGA standards for comprehensive regulation of the interstate pipeline companies. The failure of the Court of Appeals to consider the impact of its decision on the consuming public or even to acknowledge the large windfall to be gained by the pipelines suggests an insensitivity to the real policy dimensions of this case. The delicate balance between consuming and producing interests crafted by Congress in the NGPA was bludgeoned by the court below.

3. *Indifference of the Commission to the Reversal of the Decision of the Court of Appeals Demands That This Court Protect the Interests of the Consumer in Obtaining a Fair Review of Whether the Decision Below Contributes to a Stable, Rational Gas Pricing Policy.*

The decision of the Court of Appeals will result in competitive injury to gas distributors by increasing the prices for "old" flowing gas. In the past, gas consumers have relied on the Commission to monitor the marketplace and to intervene therein to assure just and reasonable prices for the consuming public.

The decision below emasculates the Commission's consumer protection role. By totally ignoring the expert and pragmatic response of the Commission in its Orders No. 58 and 98, the Fifth Circuit has concluded that virtually nothing remains of the Commission's consumer protection role after NGPA. Under that decision, the automatic eligibility of *all* pipeline production for NGPA prices renders the Commission impotent to exercise any discretionary authority over the economic consequences of transfers of gas within divisions of a pipeline company. With no support or justification in the language,

legislative history or pre-1978 gas industry practice, the validity of the Fifth Circuit's decision must be seriously questioned. This ruling produces the potentially absurd result of prices for a pipeline's own production not under contract running at higher levels than gas covered by a contract with a non-affiliated producer. No interest of the consumer in the short or long term is served by this construction of the NGPA. With this involuntary abdication of the Commission from its consumer protection role, the public's interest has been cast adrift.

If Congress intended completely to remove the consumer protection role from the Commission's area of responsibility, it certainly would have done so expressly. It is unlikely, indeed, that this important role, clearly articulated in the 1938 Act, reinforced in numerous decisions of this Court, and widely understood by Congress, would be suddenly repealed by implication.

The more plausible rationale is that the Commission retains its role to protect the public from unnecessary, non-mandatory price increases and that its decisions on intracorporate transfers which (1) protects the consumer from paying higher prices and (2) avoids large financial windfalls to pipeline producers for bookkeeping transfers of gas is the more reasonable interpretation and should be reinstated.

This Court has repeatedly recognized the authority of the Commission to fashion pragmatic solutions and develop practical methods for resolving disputed factual and legal questions in the gas pricing arena. *Permian Basin Area Rate Cases*, 390 U.S. at 803; *United Gas Improvement Co. v. Callery Properties, Inc.*, 382 U.S. 223, 228 (1965); *Atlantic Refining Co. v. the Public Service Commission of the State of New York*, 360 U.S. at 391; *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 586 (1942).

The Commission's definition of "first sale" in Section 2(21) of the NGPA "was essentially pragmatic" and reflected its expertise and knowledge of industry practice over forty years. *Cf. Permian Basin Area Rate Cases*, 390 U.S. at 803. It reached the reasonable conclusion that intracorporate transfers had no indicia of a "sale" or any other transfer for value and should, therefore, not be eligible for "first sale" treatment under NGPA. Order No. 58, *supra* at App. B-5-6.

In overturning the Commission's interpretation of the NGPA, the Court of Appeals ignored a fundamental principle of administrative law and refused to give deference to the expertise of the agency charged with administering the statute.[9] Instead, the court unilaterally substituted its own conclusion and construction of the statute. If a court is free to ignore the deliberations of the Commission and declare *ex cathedra* its own view of the public interest, a very dangerous precedent will have been set.

The absence of harmony between gas pricing policy with respect to intracorporate transfers, as presented by the Fifth Circuit, and that policy as interpreted by FERC and state authorities,[10] will be disruptive to the stable market environment necessary to protect consumers and maintain a viable, natural gas industry. Conflicting interpretations of the NGPA, together with serious erosion of the express responsibility of the Commission to protect the gas consuming public present significant legal questions necessitating review by this Court.

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[9] *Cf. Columbia Gas Development Corp.* v. *FERC*, 651 F.2d 1146, 1155 (5th Cir. 1981). The rationale of the Fifth Circuit is at best tortured. *See* Petitioner's Brief herein, at note 13.

[10] *See, e.g.*, Orders 59 and 98, *supra; Penzzoil Company Co.* v. *Public Service Commission of W. Va.*, No. 80-175-G, 42T (unreported decision of the Supreme Court of W. Va.), Petition for Writ of Certiorari No. 81-1672, filed March 10, 1982.

The Court of Appeals is not the proper forum and did not have before it an appropriate record for balancing the multitude of fact-laden public interest considerations which should at least be reviewed when dramatic shifts in gas pricing policies are at issue—*e.g.*, production, cost, supply incentives, economic impacts, etc. These are the kinds of factual considerations weighed by the Commission before issuing its orders under review in this case. Further, the Commission is clearly the forum for such a factual determination with respect to the prospective or retroactive application of the decision.

At a minimum, this case should be remanded to the Commission to exercise its discretion as to the appropriateness of retroactive application if the decision of the Court of Appeals is affirmed by this Court. *See* Order 93A, Docket No. RM80-33 (issued April 24, 1981) at p. 29.

CONCLUSION

The Fifth Circuit erred in summarily reversing the Commission's interpretation of the NGPA's definition of "first sale" as applied to intracorporate transfers. The Court of Appeals by "a stroke of the pen" has vitiated forty years of industry practice and has ignored the expertise of the Commission charged with administering the Act.

If the decision below is not reversed, it will bestow a huge windfall on natural gas pipeline producers "with a consequent squall for the consumers. This the Congress did not intend." *Atlantic Refining Co. v. Pub. Comm. of N.Y.*, 360 U.S. at 390.

Failure of this Court to grant certiorari in this case would be a serious blow to millions of natural gas consumers who have already sustained major energy cost increases under NGPA and would destroy the stability of gas pricing policy established over the past forty

years. This Court should act to preserve what remains of the Commission's role as protector of the consumer after NGPA and in so doing reverse the usurpation of the Commission's authority under the decision of the Court of Appeals.

Respectfully submitted,

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May 11, 1982

Amicus Brief

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
THE STATE OF MICHIGAN,
THE FEDERAL ENERGY REGULATORY COMMISSION,
Petitioners,

vs.

MID-LOUISIANA GAS COMPANY, ET AL.,
Respondents.

MOTION OF EDMUND G. BROWN JR., GOVERNOR OF CALIFORNIA, FOR LEAVE TO FILE BRIEF AMICUS CURIAE AND BRIEF AMICUS CURIAE IN SUPPORT OF PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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Governor of California

Edmund G. Brown Jr., Governor of California, moves for leave to file the accompanying brief amicus curiae. This motion is necessary because a party to the proceeding before the United States Court of Appeals for the Fifth Circuit refused to consent to the filing of this amicus curiae brief.

Utility rates have become a most pressing public issue in California. This state's residential, commercial, agricultural, and industrial consumers have been asked to absorb hundreds of millions of dollars in increased natural gas costs in 1982. These increases are already causing problems in every sector of California's economy.

Further increases can only exacerbate already critical economic problems. Unless overturned by this Court, the decision below will cost California consumers $200 million per year.

Governor Brown is aware of the amici curiae brief filed in this case by the California Public Utilities Commission (CPUC) in association with major California energy utilities. The Governor in no way wishes to displace the CPUC or diminish its role in this proceeding. However, the Governor's interest in this case is broader than that of the CPUC. The Governor of California holds the supreme executive power of the state, Cal.Const., art. 5, § 1, and is vested with "the civil administration of the laws of the state", Cal. Gov. Code § 11150. Ultimately, skyrocketing energy costs have a direct effect on the health and welfare of every citizen of California. This makes the Governor's interest in this case both vital and acute.

The Governor is California's "official organ of communications" with the federal government, Cal.Gov. Code § 12012. In this role, the Governor closely monitored the congressional deliberations which resulted in the enactment of the Natural Gas Policy Act (NGPA). Indeed, the Governor is aware of legislative history pertaining to the NGPA which was either unknown to or ignored by the court of appeals. This legislative history, presented in part in the accompanying amicus curiae brief, indicates that the court below has misread the NGPA, resulting in a multi-billion dollar windfall for natural gas pipeline companies and gross injustice to the business and residential consumers of natural gas in California and the nation.

Because of the Governor's acute interest in this case and his ability to provide this Court insight into the legislative deliberations which led to enactment of the NGPA, the Governor of California seeks leave to file the attached amicus curiae brief with this Court.

August 3, 1982.

Respectfully submitted,

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TABLE OF CONTENTS

	Page
Table of Authorities	iii
Opinion Below	2
Statutes Involved	2
Interest	3
Summary of Argument	4
Argument	5
I	
This Court, not a Court of Appeals, should determine the scope and operation of the Natural Gas Policy Act	5
II	
Contrary to the intent of Congress, the Court of Appeals decision results in an inequitable "double dip" into consumers' pocketbooks and windfall profits for natural gas pipeline companies	9
III	
The Court of Appeals decision is in conflict with standards established by this Court for judicial review of decisions by federal regulatory agencies	15
Conclusion	16

TABLE OF AUTHORITIES

Cases *Page*

Aetna Life Insurance Co. v. *Haworth*, 300 US 229 (1937) 9
Batterton v. *Francis*, 432 US 416 (1977) 5, 16
California v. *LoVaca Gathering Co.*, 379 US 366 (1965) 8
California v. *Southland Royalty Co.*, 436 US 519 (1978) 8
Corporation Commission of Oklahoma v. *Federal Power Commission*, 362 F.Supp. 522 (W.D.Okla) aff'd. 415 US 961 (1974) 8
Marbury v. *Madison*, 1 Cranch 137, 2 L.Ed. 60 (1803) 9
Phillips Petroleum Co. v. *Wisconsin*, 347 US 672 (1954) 8
Tenneco Oil Co. v. *Federal Energy Administration*, 613 F.2d 298 (TECA, 1979) 14

FERC Orders

Order No. 58, Docket No. RM80-7 (issued November 14, 1979) 2, 10, 15
Order No. 98, Docket No. RM80-6 (issued August 4, 1980) 10, 14, 15
Order No. 102, Docket No. RM80-7 and RM80-6 (issued October 3, 1980) 10

Statutes

Natural Gas Act, 15 USC (& Supp IV) 717 *et seq.* ..... passim
Section 4, 15 USC 717c 6
Section 5, 15 USC 717d 6
Natural Gas Policy Act of 1978, 15 USC (Supp IV) 3301 *et seq.* passim
Section 2(21), 15 USC (Supp IV) 3301(21) ..... passim
Sections 102–109, 15 USC (Supp IV) 3312–3319 6
Section 121, 15 USC (Supp IV) 3331 6
Section 122, 15 USC (Supp IV) 3332 7
Section 122(a), 15 USC (Supp IV) 3332(a) 7
Section 201, 15 USC (Supp IV) 3341 *et seq.* 7
Section 203(b), 15 USC (Supp IV) 3343(b) 7
Section 504, 15 USC (Supp IV) 3414 7
Section 504(b), 15 USC (Supp IV) 3414(b) 7
Section 504(c), 15 USC (Supp IV) 3414(c) 7

Miscellaneous

123 Cong.Rec. 32306–32308 (1977) (the text of HR 5289, as amended by the Senate) 13
124 Cong.Rec. H 13114–13115 (daily ed. October 14, 1978) (Statement of Congressman Dingell) 11, 12
H.R. Rep. No. 95-496 (Pt. 4), 95th Congress, 1st Sess. (1977) *reprinted in* 1978 U.S. Code Cong. & Ad News 8454 13
H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. (1978) *reprinted in* 1978 US Code Cong. & Ad News 8800 ..... 14, 15

No. 81-1889, No. 81-1958, No. 81-2042, No. 82-19

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
THE STATE OF MICHIGAN,
THE FEDERAL ENERGY REGULATORY COMMISSION,

Petitioners,

vs.

MID-LOUISIANA GAS COMPANY, ET AL.,

Respondents.

BRIEF AMICUS CURIAE OF EDMUND G. BROWN JR., GOVERNOR OF CALIFORNIA, IN SUPPORT OF PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Edmund G. Brown Jr., Governor of California, herewith submits his brief, amicus curiae, in support of the petitions for a writ of certiorari filed by the Public Service Commission of the State of New York (No. 81-1889), Arizona Electric Power Cooperative, Inc. (No. 81-1958), the State of Michigan (No. 81-2042), and the Federal

Energy Regulatory Commission (No. 82-19). For the reasons set forth below, the United States Court of Appeals for the Fifth Circuit erred in vacating Orders Nos. 58 and 98 of the Federal Energy Regulatory Commission in the decision reported as *Mid-Louisiana Gas Company, et al.* v. *Federal Energy Regulatory Commission*, 664 F.2d 530 (1981).

OPINIONS BELOW

The opinion of the court of appeals (Pet.App. A-1 to A-15) [1] is reported at 664 F.2d 530. The orders of the Federal Energy Regulatory Commission (Pet.App. B-1 to B-13, B-14 to B-49 and B-50 to B-82) are not reported.

STATUTES INVOLVED

1. Section 2(20) of the Natural Gas Policy Act of 1978, 15 U.S.C. (Supp. IV) 3301(20), provides:

> The term "sale" means any sale, exchange, or other transfer for value.

2. Section 2(21) of the Natural Gas Policy Act of 1978, 15 U.S.C. (Supp. IV) 3301(21), provides:

> (A) General rule
>
> The term "first sale" means any sale of any volume of natural gas—
>
> (i) to any interstate pipeline or intrastate pipeline;
>
> (ii) to any local distribution company;
>
> (iii) to any person for use by such person;
>
> (iv) which precedes any sale described in clauses (i), (ii), or (iii); and

---

[1] "Pet.App." refers to the appendix to the petition in No. 81-1889.

(v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this chapter.

(B) Certain sales not included

Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

INTEREST

As set forth in the accompanying motion for leave to file brief amicus curiae, which is incorporated herein by reference, Governor Brown has a vital interest in the outcome of this case. The Fifth Circuit's decision, if permitted to stand, may result in increased gas costs to California residential consumers, business and industry of $200 million per year. In every sector of California's energy intensive economy, this will create problems which Governor Brown will be called upon to address.

The Governor has a further strong interest in this proceeding. He is chief executive of the largest natural gas consuming state in the nation. To protect the interests of California, he closely monitored the congressional deliberations which resulted in the Natural Gas Policy Act (NGPA). The NGPA represents an intricate set of compromises between natural gas producing and con-

suming interests. Governor Brown is vitally interested in assuring that the pro-consumer elements of this legislation are protected by this Court.

SUMMARY OF ARGUMENT

The court below has interpreted the "first sale" definition of the NGPA for the first time. The immediate effect of this interpretation is to grant incentive prices to gas produced by a pipeline whether or not the pipeline risked its own money or that of its downstream customers, so-called "cost-of-service" gas. However, this interpretation will have effects far beyond the pricing of "cost-of-service" gas.

The "first sale" definition is the keystone of the NGPA. What is a "first sale" determines the operation of every major element of this Act. It is no understatement that every producer and consumer of natural gas in America is affected by what is or is not a "first sale".

The meaning, and necessarily the scope, of the term "first sale" is so fundamental to the operation of the NGPA that an early and definitive interpretation is essential. It is respectfully submitted that an opinion of this Court is necessary to guide federal authorities administering the Act, state regulators, pipelines, producers, the investment community, and consumers.

The effect of the decision of the court below is to allow a "double dip" into consumers' pocketbooks. The opinion below allows "cost-of-service" gas, for which the costs of exploration and development have already been borne by interstate consumers, the first dip, to be sold

to these same consumers at prices designed to reward those who actually bear the financial risks of finding and developing new natural gas reservoirs, the second dip. This results in unbargained for windfall profits which are manifestly unfair to consumers and contrary to the intent of Congress.

The court below erred in brushing aside the interpretation of the term "first sale" by the Federal Energy Regulatory Commission (FERC). The FERC was authorized by the NGPA to define certain terms in the Act, including the terms "first sale" and "transfer of value". The *de novo* review standard used by the court below in examining FERC's definition of these key terms has already been rejected by this Court in another case under similar circumstances. *Batterton* v. *Francis*, 432 US 416 (1977).

To correct the obvious errors and inequities in the decision of the court below, it is respectfully submitted that this Court accept jurisdiction and expedite briefing and argument in this case.

ARGUMENT

I

THIS COURT, NOT A COURT OF APPEALS, SHOULD DETERMINE THE SCOPE AND OPERATION OF THE NATURAL GAS POLICY ACT

The court below has, for the first time, interpreted the meaning and scope of the term "first sale" in the Natural Gas Policy Act (NGPA) of 1978, 15 USC § 3301(21). The

implications of this interpretation can only be understood against the backdrop of the NGPA. The "first sale" definition is at the heart of this Act. Indeed, what is a "first sale" determines both the scope of federal power over domestically produced natural gas under the NGPA and the operation of every major provision of this Act.

When there is a "first sale" of natural gas, the NGPA displaces both Natural Gas Act (NGA), 15 USC § 717 *et seq.*, price regulation of the interstate market and the power of individual states over the pricing of gas produced and consumed within their own borders, the intrastate market. Once the jurisdictional threshold of a "first sale" is crossed, the NGPA provides statutory pricing formulae for defined categories of natural gas production, 15 USC § 3312–3319. Many of these production categories are released from federal price controls on January 1, 1985, 15 USC § 3331. When there is not a "first sale" of gas, the pricing of natural gas is determined by federal authorities under the "just and reasonable" standard of the Natural Gas Act, 15 USC § 717(c) and § 717(d), or by state officials pursuant to state laws not displaced by the NGPA or NGA. Literally billions of dollars turn on which regulatory system governs a particular kind of natural gas production.

This does not end the impact of the "first sale" definition. Within the structure of the NGPA, important economic and legal decisions are keyed to what is a "first sale".

An incremental pricing provision in the NGPA allo-

cates increased natural gas costs initially to certain low priority users of gas. 15 USC § 3341 *et seq.* Costs shifted to low priority users and away from high priority users of gas consist principally of "the price paid . . . in any first sale" of gas. 15 USC § 3343(b). The extent of this allocation will substantially determine the cost of goods produced by low priority industrial gas consumers and the cost of gas to residential consumers.

The Act makes it unlawful for any person to sell gas at "a *first sale* price in excess of any applicable maximum lawful price". 15 USC § 3414 (emphasis added). A knowing violation of this prohibition triggers civil penalties of up to $5,000 for any one violation. 15 USC § 3414(b)(6). A knowing and willful violation subjects a person to a fine of not more than $5,000 or imprisonment for not more than two years, or both. 15 USC § 3414(c).

The President or Congress can extend federal price controls over natural gas after July 1, 1985 using expedited procedures contained in 15 USC § 3332. This extension authority is limited to reimposition of "maximum lawful prices for *first sales* of natural gas". 15 USC § 3332(a) (emphasis added).

In numerous decisions concerning the NGA, this Court has demonstrated an abiding commitment to careful judicial scrutiny of the implementation of federal natural gas law. This has been particularly true in cases presenting questions concerning the scope of the NGA. See *California* v. *Southland Royalty Co.*, 436 US 519 (1978), continuing obligation under NGA after lease termination; *Corporation Commission of Oklahoma* v.

Federal Power Commission, 362 F. Supp. 522 (W.D.Okla.) aff'd 415 US 961 (1974), FPC power to sue state agency allegedly interfering with its powers under the NGA; *California* v. *LoVaca Gathering Co.,* 379 US 366 (1965), NGA applicable to comingled stream of gas; and *Phillips Petroleum Co.* v. *Wisconsin,* 347 US 672 (1954), NGA jurisdiction over independent gas producers. This case presents this Court with its first opportunity to ascertain the scope of the Natural Gas Policy Act.

It is both consistent with this Court's past policies and manifestly in the public interest for this case to be reviewed. Like the many cases taken by this Court in the past concerning the NGA, this one presents the fundamental question of the scope of federal power over natural gas. Early and definitive resolution of questions concerning the scope and operation of the NGPA, all related to the meaning and scope of the "first sale" definition, are critical to the orderly administration of the NGPA. Certainty in the definition of this key term—certainty which can only be provided by a decision of this Court—is required to guide the actions of federal authorities, state regulators, producers, pipelines, and consumers in a myriad of natural gas transactions worth billions of dollars. Although it is axiomatic under the "case or controversy" doctrine that this Court will deal only with the controversy in this case, *Aetna Life Insurance Co.* v. *Haworth,* 300 US 229 (1937), it is clear that interpretation of the term "first sale" for any purpose will largely determine its meaning for every other purpose. It is respectfully submitted that this is preeminent-

ly a case in which the public-at-large needs this Court to state "what the law is". *Marbury* v. *Madison*, 1 Cranch 137, 177, 2 L.Ed. 60, 73 (1803).

II

CONTRARY TO THE INTENT OF CONGRESS, THE COURT OF APPEALS DECISION RESULTS IN AN INEQUITABLE "DOUBLE DIP" INTO CONSUMERS' POCKETBOOKS AND WINDFALL PROFITS FOR NATURAL GAS PIPELINE COMPANIES

The interpretation of the "first sale" definition in the NGPA by the court below gives "first sale" status to intracorporate transfers of gas from a pipeline company's wells to its pipeline. This interpretation necessarily grants such pipeline production the incentive prices established by the NGPA. These prices would be achieved whether the pipeline risked its own money or that of its downstream customers through previous "cost-of-service" treatment of the pipeline's exploration and development costs.

Under the "cost-of-service" methodology, pipelines expensed or capitalized prudently incurred costs in the exploration and development of natural gas reserves. Under this procedure, even dry hole and other expenses associated with unsuccessful or marginal ventures were passed through a pipeline's downstream customers. FERC Order No. 98 (Pet.App. B-26 through B-27). Thus, neither the pipeline company nor its shareholders bore the manifest financial risks of gas exploration; their customers did. Consumers were rewarded for their risk-

taking by ultimately receiving gas at cost, plus a reasonable rate of return to the pipeline.

Through the exercise of its rulemaking authority under the NGPA and exercise of its authorities under the Natural Gas Act, FERC Orders Nos. 58 (Pet.App. B-1) and 98 (Pet.App. B-14), actions set aside by the Court below, the FERC distinguished between gas produced through exploration and development financed by a pipeline's own money and "cost-of-service" gas financed by consumers. If the pipeline risked its own money, it received NGPA incentive prices. If consumers bore the financial risk of success or failure, they received gas at cost, plus a reasonable rate of return. Under this structure, both consumers and pipelines were to receive the benefits of their bargains.

With respect to cost-of-service gas, the FERC stated in its Order No. 102, reaffirming Orders Nos. 58 and 98, that:

> . . . pipelines have already enjoyed the benefits of a certain recovery of and return on the costs of production, and that their customers, who have borne the risks of this investment in the early years of exploration and development, should have an opportunity to receive the price benefits of cost-of-service treatment for gas produced as a result of these expenditures. (Pet.App. B-56 through B-57).

The actions of the FERC precluded a "double dip" into consumers' pocketbooks. The first dip arises from payment by downstream customers of the costs of exploration and development of gas; the second dip results from billing these same downstream customers for that same

gas at incentive prices designed to reward those who undertake the financial risks of exploration and development. By characterizing the transfer of gas from a pipeline's wells to its pipeline as a "first sale", the court below allows pipeline companies to take this inequitable second dip with impunity.

The costs of this second dip are staggering. Petitioner Arizona Electric Power Cooperative, Inc. suggests these costs may be many billions of dollars to consumers nationally. Petition 81-1958 at 13. In California, this second dip will cost $200 million annually. These huge sums will be transferred to natural gas pipelines which had bargained for nothing more than a reasonable rate of return. In short, this is a windfall of unprecedented proportions to pipeline companies.

This windfall is neither equitable nor consistent with the intent of Congress. According to Congressman Dingell, manager of the NGPA conference report in the House, "(t)he Natural Gas Policy Act provides reasonable price incentives, *while avoiding windfall profits*". 124 *Cong.Rec.* (Daily Ed.) Oct. 14, 1978, H 13115, (emphasis added). Speaking specifically to the new ceiling prices provided in the NGPA, Congressman Dingell explained to his colleagues:

> The bill's price ceilings increase over time to reflect inflation and, in certain instances, to spur increased investment in exploration for, and development of, our Nation's natural gas resources. *A key aspect of the conference report is the focusing of price increases on categories of production which promise the greatest supply response at the lowest*

> *cost to consumers.* The deregulation provisions provide the incentives required for producers to *undertake investments* in production projects . . . 124 *Cong.Rec.* (Daily Ed.) Oct. 14, 1978 at H 13114 (emphasis added).

Clearly, the financial rewards of the NGPA were closely targeted to those who invested in the risky business of finding and developing natural gas supplies. Just as clearly, the interpretation of the court below results in rewarding pipelines even when they did not risk their own dollars in seeking and developing new gas supplies. Indeed, the interpretation of the court below denies the benefits of investing in natural gas exploration and development to an important class of risktakers, downstream consumers who financed gas exploration and development through "cost-of-service" pricing of pipeline sales.

In reaching this odd result, the court below found that "Congress did not explain its definition of first sale either in the committee reports that acompanied the various drafts of the NGPA or in the discussions that occurred in each house" (Pet.App. A-10). Unencumbered by any legislative history directly pertaining to the "first sale" definition, the court below wrought a fictional sale and "first sale" from the whole cloth of accounting entries associated with the transfer of gas from a pipeline's wells to its transportation system.

The underlying premise of the court below that there is no relevant legislative history concerning the "first sale" definition is simply wrong. Not only is there legislative history pertaining to the "first sale" definition but

that history indicates a classic pattern of legislative give and take between the houses.

In the House of Representatives, a "first sale" was an essential condition precedent to receipt of liberalized price ceilings. According to the jurisdictional committee in the House:

> The Committee intends that the term "first sale" be applied by the Federal Power Commission to the first transfer of natural gas for value *in an arms length transaction.* Therefore, the first sale price is essentially a wellhead price. H.R. Rep. No. 95-496 (Pt. 4), 95th Cong., 1st Sess. 103, 1977, *reprinted in* 1978, U.S. Code Cong. & Ad. News 8547, (emphasis added).

Under this definition, intracorporate transfers of gas would not be first sales because they would not be arms length transactions.

In the Senate, a very different policy was developed. In addition to providing for expedited deregulation of natural gas prices, the Senate measure contained no "first sale" or other similar condition to receipt of liberalized price treatment of natural gas production. 123 *Cong.Rec.* 32306–32308 (Oct. 4, 1977). (See text of HR 5289, as amended by the Senate.)

In conference, a choice between the polar approaches of the House and Senate had to be made. One choice was to retain the "first sale" limitation of the House measure. H.R. Conf.Rep. No. 95-1752, 95th Cong. 2d Sess. (1978) *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983. On other important matters the House gave way to the Senate. For example, many categories of natural gas were

freed from federal price controls on January 1, 1985 in the final bill. *Id.* at 68–69, 1978 U.S. Code Cong. & Ad. News 8984–8985. In addition, a whole new category of gas was granted liberalized price treatment and ultimate deregulation. *Id.* Neither policy was contained in the more consumer-oriented House bill.

Implicit in the lower court's opinion is the assumption that in reducing the"first sale" limitation to legislative text the conferees changed the meaning of the term, as understood by the House, to include what it had previously precluded. No such drafting legerdemain appears from the face of the definition unless the meaning of the term sale is distorted to include what it generally does not, a transfer of product, with related bookkeeping entries, from one portion of a company to another. *Tenneco Oil Co.* v. *Federal Energy Administration,* 613 F.2d 298, 302 (TECA, 1979); FERC Order No. 98 (Pet.App. B-66).

Nothing in the conference report, H.R. Conf. Rep. No. 95-1752, *supra,* nor anything in the final debates in either house, particularly the House of Representatives, suggests that the "first sale" limitation was so altered. The only reasoned conclusion from the legislative history concerning the purposes of the NGPA and the specific history pertaining to the "first sale" definition is that an intracorporate transfer of the kind considered by the court below is not made a "first sale" by operation of the statutory definition of this term in the NGPA.

Starting from a false premise, the court below reached a false conclusion. It is respectfully submitted that this

Court should take jurisdiction in this case to rectify this error.

III

THE COURT OF APPEALS DECISION IS IN CONFLICT WITH STANDARDS ESTABLISHED BY THIS COURT FOR JUDICIAL REVIEW OF DECISIONS BY FEDERAL REGULATORY AGENCIES

The court below characterized FERC Orders Nos. 58 and 98 as interpretive regulations. This is error.

These orders were substantive regulations issued pursuant to 15 USC § 3411 (b). This provision authorizes the FERC to "define . . . technical and trade terms used" in the NGPA. *Id.* With respect to this authority, the conference report states:

> . . . the Commission may define terms such as 'transfer for value' used in the definition of first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition. H.R. Conf.Rep. No. 95-1752, *supra,* at 116, 1978 U.S. Code Cong. & Ad. News 9033.

FERC Orders Nos. 58 and 98 represent a substantive exercise of this rulemaking authority. As a consequence, the court below was "not free to set aside those regulations simply because it would have interpreted the statute in a different manner." *Batterton* v. *Francis,* 432 US 416, 425 (1977).

CONCLUSION

For the reasons set forth above, the petitions for a writ of certiorari to the Court of Appeals for the Fifth Circuit should be granted.

Dated: August 3, 1982.

Respectfully submitted,

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Amicus Brief

3

MOTION FILED
MAY 12 1982

No. 81-1889

IN THE
Supreme Court of the United States
OCTOBER TERM, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioner,
v.
MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE AND BRIEF OF AMICUS CURIAE STATE OF KANSAS AND KANSAS CORPORATION COMMISSION IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI FILED BY THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

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TABLE OF CONTENTS

	Page
Motion for Leave to File Brief Amicus Curiae	1
Interest of Amicus Curiae	3
Argument	4
1. Kansas Regulatory Treatment	4
2. Appropriate Rate Treatment is Cost of Service	5
3. The Court of Appeals decision that intracorporate transfer of pipeline produced gas are "transfer for value" and "first sales" within the meaning of the NGPA is inconsistent with their meaning and ignores FERC expertise	6
Conclusion	7

TABLE OF AUTHORITIES

Cases	Page
Mid-Louisiana Gas Company, et. al., Federal Energy Regulatory Commission and Consolidated Gas Supply Corporation v. Federal Energy Regulatory Commission, 664 F.2d 530 (1981)	2
Statutes	
Natural Gas Policy Act of 1978, 15 U.S.C. & 3301 et. seq.	4, 5, 6, 7
K.S.A. 66-101 et seq.	2, 3
Other Sources	
Rate Applications of Kansas-Nebraska Natural Gas Company, Inc.-Kansas Corporation Commission, Docket No. 132,202-U	5
Petition for Writ of Certiorari filed April 12, 1982 in Docket No. 81-1889 In the Supreme Court of the United States	6

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1889

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,

Respondents.

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

Comes now the State Of Kansas and the Kansas Corporation Commission (State Commission) and moves the Court for Leave to File the attached brief amicus curiae in this case pursuant to Supreme Court Rule 3.64. As this brief is being filed on behalf of the State of Kansas and the State Commission by the Attorney General of the State of Kansas and his Special Assistants, and by the General Counsel and Assistant General Counsel of the State Commission pursuant to Supreme Court Rule 3.64, consent of the Attorneys for the parties is not required.

The interest of the amicus State of Kansas and State Commission in this case stems from their concern over the drastically increasing costs of natural gas to the citizens of their state. The State Commission is the regulatory body responsible for regulation of utility and pipeline operations within the State of Kansas. As such, the amicus State Commission is responsible for setting rates for gas utilities and natural gas pipelines that conduct intrastate operations within the State of Kansas. The State Commission has the dual responsibility under

Kansas law to set just and reasonable rates which will allow utilities to earn a fair return on their investment and to protect the interest of the citizens of the State of Kansas from unjust and unreasonable rates. (See K.S.A. 66-101 et. seq.) Because of these responsibilities the State of Kansas and the State Commission supports the petition for a Writ of Certiorari filed by the Public Service Commission of the State of New York for a Petition for a Writ of Certiorari to review the December 23, 1981 decision of the United States Court of Appeals for the Fifth Circuit in *Mid-Louisiana Gas Company, et al. v. Federal Energy Regulation Commission*, Case No. 80-3804, and *Consolidated Gas Supply Corporation v. Federal Energy Regulatory Commission*, Case No. 80-4010 and reported in 664 F.2d 530.

The brief of the amicus State of Kansas and State Commission support the Petition for a writ by New York and points out the implications and consequences such decision may have on traditional ratemaking.

Respectfully submitted,

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IN THE

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OCTOBER TERM, 1981

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THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

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MID-LOUISIANA GAS COMPANY, *et al.*,

Respondents.

BRIEF OF AMICUS CURIAE STATE OF KANSAS AND KANSAS CORPORATION COMMISSION IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI FILED BY THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

INTEREST OF AMICUS CURIAE

The State of Kansas and the Kansas Corporation Commission have a specific interest in the consumers within the State of Kansas. The Kansas Corporation Commission is charged by state law (K.S.A. 66-101 et seq.) with the regulation of public utilities within the State of Kansas. Both the Kansas Commission and the State of Kansas are vitally concerned with the drastically increasing costs of natural gas.

The effect of the decision of the Fifth Circuit Court of Appeals impacts not only the ratepayers and citizens of

the State of Kansas, but those of the United States as a whole.

The facts of this case are concisely stated in the Statement of the Case by the Petitioner, The Public Service Commission of the State of New York and will not be repeated by the amicus. Additionally the amicus supports the arguments *and* authorities as submitted by the Petitions. It is hoped that the amicus brief will show the effect of this decision if applied to pipeline sales within the State of Kansas.

The direct effect of the decision by the Fifth Circuit Court of Appeals on Federal Energy Regulatory Commission jurisdictional interstate pipeline's is not subject at this time to direct measurement, but suffice it to say the impact can only be more drastically increasing prices tied not to cost but to NGPA Prices.[1]

ARGUMENT

1. Kansas Regulatory Treatment.

In the State of Kansas, successful drilling efforts by companies are allowed in that company's rate base. Therefore, successful efforts earn a rate of return as authorized by the Kansas Commission, are depreciated, and the company collects taxes thereon. Unsuccessful efforts in Kansas are treated as an expense item. The effect of the Court of Appeals ruling is to remove all company owned production from rate base.[2] This would

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[1] Any jurisdictional Kansas Utility who bought gas from an interstate pipeline which had its own production priced pursuant to the fifth circuit's opinion would pass those costs on to its customers through its PGA (Purchased Gas Adjustment Clause).

[2] This section of the brief assumes for argument the application of the decision in 664 F.2d 530 to Pipeline Operations over which the Kansas Commission has jurisdiction.

appear at first glance to benefit the ratepayer, i.e., the production would be removed from rate base with the company no longer earning a return on its investment or recovering depreciation or taxes. However, a close review of the practical implication of this in one case now pending before the Kansas Commission shows the same not to be true.

On February 12, 1982, Kansas-Nebraska Natural Gas Company, Inc., filed an application for a rate increase in Docket No. 132,202-U with the Kansas Corporation Commission.[3] The effect on that rate case assuming Kansas-Nebraska's requested rate of return, (13.24%) and the appropriate tax factor (1.9859) is $2,275,925. Again, this appears to benefit the ratepayers, but this is not true. The effect on Kansas-Nebraska's operating income of the allowing NGPA pricing is $3,929,032. Therefore, the overall effect of the change from cost of service treatment to NGPA pricing is $1,653,107. It should be stated that Kansas-Nebraska is requesting a total revenue increase of $7,131,829; 23.20 percent of this rate case application is this one issue alone.

2. Appropriate Rate Treatment Is Cost Of Service.

The State of Kansas and the Kansas Commission believe that cost of service treatment is the only appropriate method which can or should be utilized for ratemaking purposes. The ratepayers in Kansas on some wells already in rate base have paid a return on the company's investment, depreciation, and related taxes for

---

[3] This case is pending on the Kansas Commission's docket. Prefiled testimony indicates the departure from jurisdictional Kansas ratemaking approach is based on the Fifth Circuit Court of Appeals decision in 664 F.2d 530. Kansas-Nebraska is both an interstate pipeline and a regulated utility in the State of Kansas.

years. In other words, the ratepayers have borne the risk of the company's exploration for natural gas. The escalation to NGPA prices absent some cost justification is a windfall. Additionally, the NGPA itself refers to "maximum" lawful prices. The pipeline by escalating to NGPA prices would go the maximum of lawful prices without cost justification under the court's decision rather than the normal ratemaking approach based upon the cost of providing service. The court's ruling would have the effect of making "maximum" lawful prices the price. The cost to the utility of the product would be irrelevant as long as it did not exceed over the long haul what would be recouped through the NGPA prices. The result then could only be drastically increasing consumer prices tied not to cost, but to artificially established prices (NGPA).

3. The Court of Appeals decision that intracorporate transfer of pipeline produced gas are "transfer for value" and "first sales" within the meaning of the NGPA is inconsistent with their meaning and ignores FERC expertise.

The FERC's authority to define terms, i.e., "transfer for value" is provided by Section 501(b) 15 U.S.C. § 3411 (b) of the NGPA. Additionally, the common meaning of the term imports a contractual understanding where there are arm's length negotiations, consideration, transfer and a meeting of minds.[4] Such negotiations would be clearly present in producer pipeline purchases but the same cannot be implied to pipelines intradepartmental negotiations.

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[4] See Page 17 Petition for Writ of Certiorari Public Service Commission of the State of New York 81-1889 and the cases cited in Footnote 17.

CONCLUSION

The Court of Appeals has improperly interpreted the NGPA and found incorrect FERC interpretation. The impact of this decision at the Federal level is a drastic increase in natural gas prices. The importance of this matter if applied to individual state ratemaking is additionally quite dramatic and reflects a departure from the proper cost of service treatment.

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MOTION FILED
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Nos. 81-1889, 81-1958, 81-2042 and 82-19

IN THE

Supreme Court of the United States

October Term, 1982

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondent.

ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondent.

STATE OF MICHIGAN,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondent.

FEDERAL ENERGY REGULATORY COMMISSION,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondent.

MOTION OF THE NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION FOR LEAVE TO FILE BRIEF AMICUS CURIAE AND BRIEF AMICUS CURIAE IN SUPPORT OF PETITIONS FOR A WRIT OF CERTIORARI

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August 4, 1982

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STATE OF MICHIGAN,
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No. 82-19

FEDERAL ENERGY REGULATORY COMMISSION,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, et al.,
Respondent.

MOTION OF NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

The National Rural Electric Cooperative Association (NRECA) respectfully moves this Court for leave to file the accompanying Brief Amicus Curiae in support of the above-captioned petitions for a writ of certiorari. This motion is necessary because the consent of certain of the respondents to file such a brief has been refused.

NRECA has approximately 1,000 members serving more than 25 million rural electric consumers in 46 states. It has a direct and substantial interest in this case because many of its member cooperatives are served by federally regulated interstate gas pipelines or state regulated intrastate pipelines and local distribution companies. The Federal Energy Regulatory Commission (FERC) promulgated Orders 58 and 98 in a rulemaking proceeding. Order 58 provides that natural gas produced by interstate and intrastate pipelines and local distribution companies generally is not subject to regulation under the Natural Gas Policy Act (NGPA), 15 U.S.C. 3301, *et seq.*, because such gas is not the subject of a statutory "first sale." In Order 98, the FERC ruled that gas produced by a pipeline from a well which had ever been priced on a cost of service basis must always be subject to such treatment.

The Court of Appeals' decision overturning these orders will have a substantial effect on NRECA's members and their customers. Many NRECA members use pipeline produced gas to generate electricity and others purchase electricity generated with such gas. Under federal cost of service regulation, gas consumers paid the pipeline's operating expenses, taxes, depreciation and a return on investment without regard to the success of gas exploration and development ventures. If the ventures were successful, the

consumers obtained the gas on a cost plus profit basis. If it failed, the consumer bore the cost of the failure. The pipeline had no investment "at risk" in either case.

The exact dollar impact of the *Mid-Louisiana* decision on NRECA's members and the 25 million consumers they serve cannot be determined. The various petitions for certiorari filed here, however, show impacts ranging from $100 million annually (FERC Petition, p. 15, ftn. 11) to a possible $12 billion over the life of the affected reserves (Arizona Electric Power Cooperative, Inc. Petition, p. 13). This substantial increase in the price of natural gas will have a detrimental impact on NRECA's members and their customers. Fuel cost is one of the major components of electric generating costs. Not only will the increases in fuel cost be passed directly through to electric customers, but the value and utility of the NRECA members' substantial investment in gas fired utility plant will be diminished.

NRECA respectfully submits that these factors are relevant to the disposition of the petitions for certiorari by this Court and that the interests of its member cooperatives and the more than 25 million consumers they serve are not otherwise adequately represented.

WHEREFORE, NRECA respectfully requests this Court to grant it leave to file a Brief Amicus Curiae in support of petitioners.

Respecfully submitted,

Wallace Tillman

August 4, 1982

IN THE

Supreme Court of the United States

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No. 82-19

FEDERAL ENERGY REGULATORY COMMISSION,
Petitioner,

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MID-LOUISIANA GAS COMPANY, et al.,
Respondent.

BRIEF OF NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF PETITIONS FOR CERTIORARI

Pursuant to Rule 36.4 of this Court, the National Rural Electric Cooperative Association respectfully submits

this brief amicus curiae in support of the petitions for a writ of certiorari filed by The Public Service Commission of the State of New York (No. 81-1889), Arizona Electric Power Cooperative, Inc. (No. 81-1958), the State of Michigan (No. 81-2042) and the Solicitor General of the United States on behalf of the Federal Energy Regulatory Commission (No. 82-19). For the reasons set forth below, we believe that the Court of Appeals erred in reversing Orders 58 and 98 of the Federal Energy Regulatory Commission which, respectively:

1. Provide that natural gas produced by interstate and intrastate pipelines and local distribution companies generally is not subject to regulation under the NGPA because such gas cannot be the subject of a statutory first sale, and
2. Provide that pipeline produced natural gas from wells which have ever been subjected to cost of service treatment shall continue to receive cost of service treatment forever.

Each of these petitions seeks review of the decision of the United States Court of Appeals for the Fifth Circuit in *Mid-Louisiana Gas Co.* v. *FERC,* 664 F.2d 530 (1981).

INTERESTS OF AMICUS CURIAE

As set forth in the accompanying Motion for Leave to File a Brief Amicus Curiae, which is incorporated herein by reference, NRECA's members serve more than 25 million rural electric consumers. Both the member cooperatives and the ultimate consumers they serve have a vital interest in the outcome of this litigation. The Court of Appeals' decision, if not reversed, will result in an increase of substantial, but undetermined, amounts annually in the price of electricity sold by NRECA's members to their customers and will diminish the value and utility of the substantial investment in gas-fired generation equipment made by NRECA's member

cooperatives. In addition, it will force the cooperatives to use oil as a substitute fuel, in direct contravention of an established national policy of minimizing dependence on oil imports.

REASONS FOR GRANTING THE WRIT

Petitioners, The Public Service Commission of the State of New York (pp. 17-20), Arizona Electric Power Cooperative, Inc. (pp. 12-13), the State of Michigan (pp. 8-9) and the Federal Energy Regulatory Commission (p. 15) have argued that this is a case of exceptional importance to natural gas and electric consumers in the United States because of its severe economic impact. NRECA agrees with and supports these arguments, as well as the additional reasons cited by each petitioner for granting the writ.

In addition, NRECA submits that the decision in *Mid-Louisiana* will result in the very increased use of fuel oil as a substitute for natural gas in industrial applications and electric generation which Congress and the various administrative agencies of the federal government are trying to prevent.

The Omnibus Budget Reconciliation Act of 1981 repealed Section 301(a) of the Powerplant and Industrial Fuel Use Act of 1978 (PIFUA). Section 301(a) of PIFUA had prohibited the use of natural gas by existing electric powerplants after 1990 and had limited its use to certain "base period" volumes until that date. In repealing this Section of PIFUA, the House Committee on the Budget stated[1] that "the currently available surplus of natural gas can be used effectively to offset some of the imported oil consumed for power generation."

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[1]Omnibus Reconciliation Act of 1981, Report of the Committee on the Budget, House of Representatives to Accompany H.R. 3982, Vol. II, p. 7.

Achievement of this national goal, however, is not simply a matter of repealing a legislative prohibition on the use of natural gas. Rather, in the absence of prohibitive regulation, it depends almost entirely on the relative price of natural gas and fuel oil. If the price of natural gas exceeds the price of fuel oil, those utilities with dual fuel capability[2] will use oil. Those utilities without such capabilities will purchase power from other utilities generating with oil.

The most current available data shows that natural gas delivered to ultimate consumers cost $3.10 per million BTUs[3] in February 1982, and No. 6 high sulfur residual fuel oil cost $3.93 per million BTUs. The same publication shows that natural gas prices have risen 59.8% since January, 1980, while average high sulfur No. 6 fuel oil prices have risen only 14.4%.[4] The additional increases in natural gas prices which will result from the implementation of the *Mid-Louisiana* decision will cause natural gas prices on many pipeline systems to equal or exceed No. 6 oil prices within a short time.

Congress is not alone in encouraging the use of natural gas as a substitute for imported fuel oil. As early as March, 1979, the Economic Regulatory Administration issued rules under the authority granted it by the Department of Energy Organization Act "designed to encourage and facilitate the filing of applications by interstate pipeline companies to transport natural gas to displace fuel oil." (44 F.R. 20399).

---

[2]Utilities with both oil and gas fired units, or with one or more generating units capable of burning both fuels.

[3]Monthly Energy Review, DOE/EIA-0035 (82/06), pp. 86-87.

[4]Since 1976, average wellhead prices for natural gas have risen 310% while average No. 6 oil prices have risen only 161%. *Id.*

The preamble to the interim final rule on such transportation stated (44 F.R. 20398):

> This rule is intended to facilitate the transportation of gas used to displace fuel oil. Due to the immediate need to implement this rule as a means of reducing the nation's reliance on imported oil, we have waived the usual procedural requirements ...

The "Background" to the rule set forth these objectives even more clearly (44 F.R. 20399):

> It is essential that the Nation immediately reduce its reliance on imported oil. The need to protect the Nation's security of energy supplies and economic well-being, as well as the need to reduce the Nation's balance of payments deficit and the domestic inflation rate requires immediate action. Expanded use of natural gas would be a significant step toward reducing our short term oil consumption. Increased use of gas would help the United States meet its commitment to reduce its demand for imported oil together with the other member nations of the International Energy Agency. Increased gas use would not only help protect the Nation from the effect of any oil shortages but also would serve to cushion the increasing world oil prices, which have a detrimental effect on the Nation's balance of payments and domestic inflation rate.

ERA also developed a "Special Public Interest Exemption" program — for the same reasons — which permitted utilities and large industrials to burn gas in

excess of those volumes allowed by PIFUA. The first notice of this proposed exemption was given in January, 1979 [44 F.R. 1694]—five months before PIFUA became effective. In this notice, the ERA stated:

> The near-term use of additional natural gas and propane instead of middle distillate and other fuel oils will tend to reduce oil imports. Such shifts can also improve air quality, particularly in urban areas, ease the pressure on middle distillate supplies and increase inter-fuel competition.
>
> In these circumstances the Department of Energy encourages natural gas users who have switched from natural gas to petroleum, particularly middle distillates, as well as other industrial users of middle distillates, to switch to natural gas or propane where practicable and allowed by State or other governing laws and regulations.
>
> ***
>
> DOE seeks immediate reduction of the use of middle distillates (including kerosene-base jet fuel) in existing facilities, including electric utility gas turbines. To the extent even more natural gas is or becomes available than is necessary to replace middle distillates, national energy policy favors its use to replace heavy fuel oil imports.

On April 9, 1979, ERA issued the special exemption rules. Over 1,000 special exemptions were subsequently issued to utilities engaged in electric generation across the country.

The Federal Energy Regulatory Commission has also recognized the desirability of substituting natural gas for imported fuel oil, and taken steps to achieve that objective. On May 25, 1979, the FERC published its Final Rule on transportation certificates for Natural Gas for the Displacement of Fuel Oil. The preamble to its findings stated:

> Several existing functions within the Commission's jurisdiction will assist in displacing fuel oil with natural gas. The most important method of reducing fuel oil consumption will be by reducing (or halting any further deterioration of) curtailment levels on interstate pipelines. The objective of maximizing interstate pipeline supplies was advanced by Secretary of Energy James R. Schlesinger:
>
> > The Department will undertake two approaches to reduce imports in the near term through movements of surplus gas to oil users. The first approach is to encourage sales from producers or intrastate pipelines to interstate pipelines and distribution companies. Such sales will increase general system supply, thereby reducing overall gas curtailments and displacing fuel oil. The second approach is to encourage and facilitate the transportation of natural gas purchased directly from producers or intrastate pipelines by users capable of substituting gas for oil. In general, the Department's first priority is to encourage additions to interstate pipeline system

> supplies. However when surplus gas is not fully utilized by interstate pipelines, the transportation of direct purchases will be facilitated.[4]
>
> The Commission believes that the Secretary is correct in giving first priority to encouraging additions to interstate system supplies; direct sales to users capable of substituting fuel oil for natural gas generally must yield on calls on available gas by customers served from system supply. Our actions in the rulemaking are intended to fit the fuel oil displacement program to that order of priorities. [44 F.R. 30314; footnote omitted].

It is clear that the decision of the Fifth Circuit in *Mid-Louisiana* will destroy this important national policy goal. There is no doubt that electric utilities will use the cheapest available fuel, whether that is oil or gas. The fact is that gas prices have more than tripled in the past six years and the repricing of tens of billions of cubic feet of natural gas from a cost of service basis to an NGPA basis will accelerate these price increases.

For this reason, NRECA submits that this case is one of exceptional importance, not only in terms of the monetary impact upon natural gas consumers, which is unusually great, but in terms of an important national policy goal. As was pointed out by various petitioners, there is no clear mandate in the NGPA or the legislative history of that Act which compels the conclusion reached by the Court of Appeals. Given that fact, the determination of whether this case warrants review by this Court should include consideration of whether the consequences of *Mid-Louisiana* are in accord with, or — as is the case — frustrate an important national policy goal.

ARGUMENT

NRECA joins in and supports the arguments made by The Public Service Commission of the State of New York, Arizona Electric Power Cooperative, Inc., the State of Michigan and the Federal Energy Regulatory Commission in their respective petitions for a writ of certiorari.

Respectfully submitted,

Wallace Tillman

CERTIFICATE OF SERVICE

I, Arnold D. Berkeley, a member of the Bar of this Court, do hereby certify that, on behalf of Arizona Electric Power Cooperative, Inc., I have this day served, in accordance with Rule 28 of the Rules of the Supreme Court of the United States, three copies of the foregoing petition for a writ of certiorari, and the appendix thereto, by first class mail, postage prepaid, upon the following:

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5

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No. 81-1889 and No. 81-1958

In the Supreme Court of the United States

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THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

and

ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
Petitioners

v.

MID-LOUISIANA GAS COMPANY, et al.,
Respondents

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

AMICUS CURIAE BRIEF IN SUPPORT OF THE GRANT OF A WRIT OF CERTIORARI ON BEHALF OF THE COMMONWEALTH OF PENNSYLVANIA AND THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

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TABLE OF CONTENTS

	PAGE
Interest of Amicus Curiae	1
Summary of Argument	2
Argument:	
I. The Court of Appeals decision incorrectly confers NGPA maximum ceiling prices on commingled pipeline-produced gas	3
II. The designation of intracorporate transfers of gas as "first sales" could lead to significant increases in the cost of both interstate and intrastate natural gas to Pennsylvania purchasers and consumers	6
Conclusion	8

TABLE OF CITATIONS

CASES:

Batterton v. Francis, 432 U.S. 416 (1977)	5
Canadian River Gas Co., 3 F.P.C. 32 (1942), aff'd sub nom., Colorado Interstate Gas Co. v. FPC, 324 U.S. 581 (1945)	4
Pipeline Production Area Rate Proceeding, 42 F.P.C. 738 (1969), aff'd sub nom., City of Chicago, Ill. v. FPC, 458 F.2d 731 (D.C. Cir. 1971), cert. denied, 405 U.S. 1074 (1972)	4

STATUTES:

Natural Gas Act, 15 U.S.C. §§717a, et seq. 4

Natural Gas Policy Act of 1978 U.S.C. §§3301 et seq. 3

Section 2(20), 15 U.S.C. §3301(20) 3

Section 2(21)(B), 15 U.S.C. §3301(21)(B) .. 3

Section 103, 15 U.S.C. §3313 7

Section 108, 15 U.S.C. §3318 7

Section 501, 15 U.S.C. §3411 ..... 3, 5

Section 602, 15 U.S.C. §3432 6

FERC ORDERS:

Order No. 58, Docket No. RM80-7 (issued November 14, 1979) 3

Order No. 98, Docket No. RM80-6 (issued August 4, 1980) 4

INTEREST OF AMICUS CURIAE

Substantial quantities of natural gas delivered by interstate pipelines are consumed by residential, commercial and industrial customers located in the Commonwealth of Pennsylvania. The December 23, 1981 decision of the United States Court of Appeals for the Fifth Circuit in *Mid Louisiana Gas Company et al. v. Federal Energy Regulatory Commission,* Case No. 80-3804, and *Consolidated Gas Supply Corporation v. Federal Energy Regulatory Commission,* Case No. 80-4010, which classifies intracorporate transfers of gas as "first sales", is incorrect and threatens consumers of natural gas in Pennsylvania with significant increases in their gas utility bills. The Commonwealth of Pennsylvania and the Pennsylvania Public Utility Commission join with the Public Service Commission of the State of New York, an intervenor-respondent in the court below and Arizona Electric Power Cooperative, Inc., in urging the Court to grant the requested writ of certiorari.

SUMMARY OF ARGUMENT

The Court of Appeals has found that intracorporate transfers of pipeline-produced gas are "transfers for value" and "first sales" within the meaning of the NGPA. This holding is inconsistent with the common meaning of those terms and ignores the FERC's expertise in administering and interpreting the NGPA. The Court of Appeals decision makes NGPA maximum ceiling prices available to pipeline-produced gas that has historically been priced on a cost-of-service basis. Pennsylvania purchasers and consumers of gas could experience significant increases in the cost of natural gas because of the decision.

ARGUMENT

I. The Court of Appeals Decision Incorrectly Confers NGPA Maximum Ceiling Prices on Commingled Pipeline-Produced Gas

The Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. §§3301 *et seq.*, established a series of maximum lawful ceiling prices for "first sales" of natural gas. The NGPA at Section 2 (20), 15 U.S.C. §3301 (20) defines the term "sale" as meaning any "sale, exchange, or other transfer for value." Section 2 (21) (B) of the NGPA, 15 U.S.C. §3301 (21) (B) excludes from first sales "the sale of any volume of natural gas by an interstate pipeline . . . unless such sale is attributable to volumes of natural gas produced by such interstate pipeline." These Sections of the NGPA state only that *some* interstate pipeline production of gas may be susceptible to classification as "first sale" gas.

The Federal Energy Regulatory Commission (FERC) possesses the authority provided in Section 501, 15 U.S.C §3411, to interpret and administer the NGPA. Acting pursuant to that authority, the FERC in Order No. 58 (App. B-2) limited pipeline-produced "first sale" gas to that sold off-system at the wellhead or some other discrete sale of pipeline gas.[1] This interpretation of the NGPA by the FERC gives effect to the common meaning of "sale" and

[1] Appendix references refer to the Appendix filed in connection with the petition for a writ of certiorari of the Public Service Commission of the State of New York at No. 81-1889.

"transfer for value". The "first sale" designation therefore did not apply to pipeline-produced gas which was transferred to another division of the pipeline and commingled with gas obtained from affiliated and independent producers. FERC Order No. 98 (App. B-25-27) clarified the impact of the NGPA on policies developed under the Natural Gas Act, 15 U.S.C. §§717a, *et seq.*, by continuing historic cost-of-service pricing for gas produced from pre-1973 wells on pre-October 8, 1969 leases. The preservation of cost-of-service pricing for this gas maintained an important element of basic fairness for pipeline customers. However, Order No. 98 permitted NGPA maximum ceiling prices to apply to gas from newer wells and leases.

The cost-of-service prices charged by pipelines to their customers consist of costs plus a reasonable rate of return. *Canadian River Gas Co.*, 3 F.P.C. 32 (1942), *aff'd sub nom., Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581 (1945). Included within this cost-of-service price are the costs of both successful and unsuccessful pipeline production efforts. *Pipeline Production Area Rate Proceeding*, 42 F.P.C. 738 (1969), *aff'd sub nom., City of Chicago, Ill. v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972). Pipeline customers, including those in Pennsylvania, have consequently been absorbing for many years the financial risks associated with pipeline-produced gas. By maintaining the distinction between wellhead sales of pipeline-produced gas and that which is commingled with gas from other sources, the FERC prevented classification of the latter as "first sale" gas which is entitled to higher NGPA ceiling prices.

The FERC's distinction between discrete sales of pipeline-produced gas sold to other pipelines, ultimate consumers or distributors and gas produced and then transferred

within a pipeline corporation has been rejected by the Court of Appeals. By finding that an intracorporate transfer of gas from a production division of a pipeline corporation to its transportation division can be a "first sale", the Court of Appeals has conferred NGPA ceiling prices on gas which cannot have a price set by arms-length negotiation. NGPA maximum ceiling prices are thus available to gas historically produced and priced on a cost-of-service basis.

The Court of Appeals decision compels the FERC to find that intracorporate transfers of gas are a "transfer for value" and "sale". This holding cannot be correct. It is inconsistent with the common meaning of both of these terms. Further, it ignores the FERC's authority and expertise in administering and interpreting the NGPA. The FERC's authority to define terms such as "transfer for value" is specifically provided by Section 501(b), 15 U.S.C. §3411(b) of the NGPA. The Court of Appeals should not exercise discretion or authority to intrude into such a matter of substance in search of an alternative interpretation of a statute. *Batterton v. Francis,* 432 U.S. 416, 425 (1977).

In summary, users of natural gas in Pennsylvania have long been absorbing a portion of the pipelines' costs regardless of the degree of production success. The Court of Appeals' decision confers NGPA maximum ceiling prices on gas whose production risk, due to cost-of-service pricing, was considerably less than that experienced by independent gas producers. These ceiling prices will improperly be passed on to gas retailers and customers in Pennsylvania should the decision of the court below continue to stand.

II. The Designation of Intracorporate Transfers of Gas as "First Sales" Could Lead to Significant Increases in the Cost of Both Interstate and Intrastate Natural Gas to Pennsylvania Purchasers and Consumers

The Court of Appeals decision to include intracorporate transfers of gas within the NGPA definition of "first sales" poses the threat of higher gas prices to purchasers and consumers of natural gas in Pennsylvania. In the most recent 12 month period for which statistics are available, Pennsylvania consumers of gas purchased over 550 million Mcf from out-of-state pipelines at a cost of over $1.5 billion. The Court of Appeals decision has the effect of permitting a portion of this gas to leap to NGPA maximum ceiling prices. Although no precise quantification is possible at this time, the impact on Pennsylvania of broadening "first sales" to include intracorporate transfers of gas is thus likely to be significant.

The decision below could also impact on the price of natural gas produced in Pennsylvania for use by Pennsylvania consumers. Approximately 30 Pennsylvania gas utilities engaged in the distribution of natural gas also produce approximately 23 million Mcf of natural gas annually.[2] This gas production reaches consumers essentially through the same kind of intracorporate transfer deemed by the Court of Appeals to be a "transfer for value". Should

[2] Section 602 of the Act, 15 U.S.C. §3432, does reserve to the States the power to set prices for intrastate gas production below the NGPA ceiling prices even when a "first sale" of gas has occurred. This power however, has been challenged through the pending petition for a writ of certiorari filed by Pennzoil Company at No. 81-1672 seeking review of the decision rendered by the Supreme Court of Appeals of West Virginia.

NGPA ceiling prices apply to this gas, its cost to Pennsylvania consumers will increase approximately by $20 million.[3] As wellhead prices for NGPA categories of gas are scheduled to increase monthly until deregulation, this $20 million increase in the cost of gas is only the initial surge in gas prices that may be experienced by Pennsylvania consumers.

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[3] This gas falls within two categories of NGPA prices, Section 103 (new, onshore production wells) and Section 108 (stripper well natural gas), 15 U.S.C. §§3313, 3318. The March 1982 applicable NGPA ceiling prices for these types of gas are $2.608 per Mcf and $3.281 per Mcf respectively. The current approximate cost of this gas is $2.00 per Mcf.

CONCLUSION

The Court of Appeals has improperly expanded the availability of NGPA maximum ceiling prices to all pipeline-produced gas. This decision incorrectly ignores the authority and expertise of the FERC in interpreting and administering the NGPA. The importance of this case is evident from the impact it will have on the prices paid by purchasers and consumers of gas in Pennsylvania. The Commonwealth of Pennsylvania and the Pennsylvania Public Utility Commission urge the Court to grant the petitions for writ of certiorari filed by the Public Service Commission of the State of New York and Arizona Electric Power Cooperative, Inc.

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Amicus Brief

6

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IN THE

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ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
STATE OF MICHIGAN,
Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Petitions for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF AMICUS CURIAE OF PUBLIC POWER GROUP IN SUPPORT OF PETITIONS FOR WRIT OF CERTIORARI

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TABLE OF CONTENTS

	Page
Interest of Amicus Curiae	2
Summary of Argument	3
Argument	4
Conclusion	8

TABLE OF AUTHORITIES

Cases:

Colorado Interstate Gas Co. v. F.P.C., 324 U.S. 581 (1945) 4

Consumer Energy Council v. F.E.R.C., 673 F.2d 425 (D.C. Cir. 1982) 4

F.P.C. v. Hope Natural Gas Co., 320 U.S. 591 (1944) 4

Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672 (1954) 4

Statutes:

Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. § 717 *et seq.* 3, 4, 5, 6

Natural Gas Policy Act, 92 Stat. 3350, 15 U.S.C. § 3301 *et seq.* (Supp. IV 1980) 2, 3, 4, 5, 6

Omnibus Budget Reconciliation Act of 1981, P.L. 97-35, 95 Stat. 614 7

Powerplant and Industrial Fuel Use Act, P.L. 95-620, 92 Stat. 3289 7

Miscellaneous:

DOE, Economic Regulatory Administration, Public Interest Exemption Option Analysis (Feb. 21, 1980) 7

DOE, Economic Regulatory Administration, Order Granting Exemptions (Mar. 4, 1980) 7

H.R. Rep. No. 97-158, 97th Cong., 1st Sess., Vol. II 7

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BRIEF AMICUS CURIAE OF PUBLIC POWER GROUP IN SUPPORT OF PETITIONS FOR WRIT OF CERTIORARI

Pursuant to the provisions of Rule 36.4, the Public Power Group[1] respectfully submits this brief amicus curiae in support of the petitions for a writ of certiorari heretofore filed by the Public Service Commission of the State of New York (No. 81-1889), Arizona Electric Power Cooperative, Inc. (No. 81-1958), and the State of Michigan (No. 81-2042), all of which seek review of

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[1] The individual members of the Group—each of which is a political subdivision of a State—are listed on the inside front cover of this brief.

the judgment of the United States Court of Appeals for the Fifth Circuit in *Mid-Louisiana Gas Co.* v. *Federal Energy Regulatory Commission*, 664 F.2d 530.

INTEREST OF AMICUS CURIAE

Amicus Public Power Group consists of more than fifty municipal and other publicly owned energy systems, each of which provides electric or natural gas service to its citizens. The electricity is generated in part, and the natural gas service is provided, by natural gas purchased from various pipeline companies, and the cost of the gas thus purchased forms an important element of the rates which members of the Public Power Group charge their customers. In 1981, members of the Group served more than 2,300,000 customers in fourteen States; in providing this service, they purchased in excess of 130,000,000 Mcf of natural gas.

The decision of the court below, vacating the result reached by the Federal Energy Regulatory Commission, would reverse more than four decades of consistent regulatory practice, and require the agency to allow a pipeline to price its own long-dedicated gas production at the incentive levels which the Natural Gas Policy Act of 1978 provides for purchases from independent producers. The effect of the decision—not addressed by the court below—will be to raise gas costs substantially for customers of pipelines having their own production, without in any way providing the exploration incentive that the NGPA levels were designed to achieve. This windfall for the affected pipelines will be paid for by sharp and unwarranted increases in the gas costs of members of the Public Power Group, forcing them to increase the rates to their customers, or, in those cases where the unwarranted increases push the price of gas above the price of competing fuel, force an increased reliance on foreign oil, contrary to articulated national energy policy.

SUMMARY OF ARGUMENT

This case raises the novel and important issue whether the Federal Energy Regulatory Commission's long-recognized ratemaking jurisdiction over pipeline-produced gas under the Natural Gas Act of 1938 was, as the court of appeals held, impliedly repealed by the Natural Gas Policy Act of 1978. Because the decision of the court below, which rests on an incorrect, incomplete, and incongruous interpretation of the statutory language and admittedly finds no support in the legislative history, will result in unwarranted rate increases for the nation's gas and electric consumers and will, in this important area, preclude the Commission from considering national energy policy in administering its functions under its organic statutes, review by this Court is required.

Moreover, in arriving at its erroneous result, the court below committed two serious errors—each warranting intervention and correction by this Court—bearing on the proper relationship between a federal agency and a reviewing court of appeals. First, the court below failed to accord deference to the agency's interpretation of the statute under which it operates. Second, assuming *arguendo* that the court's finding of administrative error was sustainable, the court overstepped its authority in failing to remand to the agency to permit it to make appropriate findings in light of the newly declared judicial interpretation of the law.

ARGUMENT

I.

The petitions for certiorari present an important issue of first impression, whose resolution will bear significantly on the Commission's discharge of its duties under the Natural Gas Act and the Natural Gas Policy Act. For more than forty years, the Commission (and its predecessor, the Federal Power Commission) have priced natural gas produced by interstate pipelines primarily on a cost-of-service basis; such regulation has long been endorsed by this Court, see *Colorado Interstate Gas Co.* v. *F.P.C.*, 324 U.S. 581 (1945); *F.P.C.* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944).

The Natural Gas Policy Act of 1978 was the complex product of a bitterly contested compromise proposed to solve the problems thought to inhere in continued regulation of independent producers (*not* pipeline producers) pursuant to this Court's holding in *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954). Adopted as part of a broader package (the "National Energy Act"),[2] the NGPA rejected both outright deregulation and continuation of existing producer regulation in favor of Congressionally fixed maximum prices for different categories of gas. There is not a word in the NGPA or in its extensive legislative history, however, that indicates that Congress intended to strip the Commission of its long-held and consistently exercised power to fix the allowance for pipeline-produced gas on a cost-of-service basis; indeed, the merits *vel non* of such a dramatic change are, as the court below conceded, nowhere discussed in the committee reports or in the debates.[3]

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[2] For an illuminating discussion of the legislative history, see the opinion of Judge Wilkey for the court in *Consumer Energy Council* v. *F.E.R.C.*, 673 F.2d 425 at 435-36 (D.C. Cir. 1982).

[3] As the court of appeals rightly noted, 664 F.2d at 536:

> "The legislative history of section 3301(21) does not illuminate this issue. Congress did not explain its definition of first

With passage of the NGPA, the Commission's principal function, in terms of its natural gas jurisdiction, has been to coordinate its regulation under its two organic statutes—the NGA of 1938 and the NGPA of 1978—consistent with declared national energy policy. In the orders vacated by the court of appeals, the Commission had purported to carry out those responsibilities, continuing cost-of-service pricing for pipeline production previously accorded such treatment, and allowing the NGPA's independent-producer ceilings for certain pipeline production where the pipeline (rather than the ratepayer) had historically borne the risks of exploration. Without giving consideration to the energy policy factors considered by the Commission—indeed, implicitly holding that the Commission's consideration of such factors was irrelevant—the court of appeals held that as a result of passage of the NGPA, "the Commission lacked authority to set prices for interstate pipeline production under the NGA," 664 F.2d at 538.

II.

In holding that the 1978 Act stripped the Commission of its authority to set prices for pipeline production under the 1938 Act, the court below committed a series of major legal errors, reading a "clear meaning" into the statute that is unsupported by the statutory language, ignoring other statutory language, and creating a result that clearly was not intended by Congress.

First and foremost, the concept of pipeline production cannot be forced into an NGPA Section 2 "sale" or "first sale" mold, as the decision below proposes. A producing pipeline's delivery of gas from its own well into its transmission system is not a "transfer" of ownership, nor is it "for value", the two prerequisites of a "sale" under

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sale either in the committee reports that accompanied the various drafts of the NGPA or in the discussions that occurred in each house."

Section 2(20). Further, the "unless" clause of Section 2(21)(B), upon which the court of appeals so heavily relied, relates to a sale "*by* any interstate pipeline", i.e. a transfer to a second party for value, not a sale to a pipeline. In focusing on the trees, the decision below not only lost the forest, but misapprehended the trees as well. In straining to give an unnatural and unexpected meaning to the "unless" clause, the court overlooked its obvious purport: where, as frequently occurs, a pipeline produces gas at a point distant from its pipeline system, it normally sells such production to a second party; the "unless" clause permits such off-system sale to enjoy "first sale" status under the NGPA.

Congress was well aware that passage of the NGPA would modify the jurisdiction of the Commission under the Natural Gas Act, and in Title VI of the NGPA—and specifically in Section 601—Congress set out those areas where jurisdiction was being terminated. Significantly, jurisdiction over pipeline production was not one of the areas deleted.

Given the long history of Commission-determined cost-of-service regulation for pipeline production—a history which antedated and is separate from the cost-of-service regulation of independent producers—it is simply beyond belief that Congress would, without a word of discussion or debate, have terminated such regulation through an obscure proviso in a definitional section of the 1978 legislation.

The court below further erred in refusing to accord deference to the FERC's interpretation of its own statute, despite the fact that, in the NGPA, Congress explicitly gave the Commission authority "to define, by rule, accounting, technical, and trade terms used in this Act," see NGPA, Section 501(b). And, even assuming that its legal conclusions were correct, the court erred in its remedy by failing to remand to the agency to determine whether, if these intracorporate transfers are to be

treated as "first sales", they should be subject to contract price limitations.

III.

While it is not possible, at this point, to calculate the ultimate dollar impact of the court of appeals' decision, pipeline claims based on the decision below already are in the hundreds of millions, and ultimate claims over the remaining life of affected reserves will almost certainly be in the billions. Increases of this magnitude—which, it should be noted, are a bonus for gas long-discovered and long-dedicated to interstate commerce and hence provide no incentive for new exploration—will not only result in otherwise avoidable increases in the costs of utility services, adding to inflationary pressures, but will, in many instances, preclude the continued purchase of gas. For members of the Public Power Group, the sharply higher prices resulting from the court of appeals' holding could well force a shift away from gas to imported oil, contrary to stated national energy policy.[4] The court

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[4] The current policy is reflected in the Omnibus Budget Reconciliation Act of 1981, § 1021(a), P.L. 97-35, 95 Stat. 614. The 1981 Act repealed Section 301(a) of the Powerplant and Industrial Fuel Use Act of 1978, which had placed limitations on the use of natural gas to generate electricity; even under the 1978 Act, however, a public interest exemption was recognized pursuant to which the Department of Energy had, on a case-by-case basis, authorized the use of natural gas to further national energy policy, see, e.g., DOE, Economic Regulatory Administration, Public Interest Exemption Option Analysis (Feb. 21, 1980), p. A. 7 ("it is in the national interest to substitute domestic natural gas for expensive, imported oil"); DOE, Economic Regulatory Administration, Order Granting Exemptions (Mar. 4, 1980), pp. 16-17 ("It is essential that the Nation immediately reduce its reliance on imported oil. . . . Expanded use of natural gas [to generate electricity] would be a significant step . . . to reduce [U.S.] demand for imported oil").

In repealing outright the limitations imposed by the 1978 Act, Congress gave explicit recognition to the type of policy considerations relied on by DOE in its Public Interest Exemption Orders under the 1978 Act, see House Budget Committee Report, H. Rept. 97-158, Vol. II, pp. 6-8.

of appeals thus effected a significant change in an important energy program without consideration of either its impact or its relationship to overall national energy policy.

CONCLUSION

For the reasons set forth above, the Public Power Group respectfully requests that the petitions for a writ of certiorari be granted.[5]

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June 1982

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[5] Amicus has been advised that a petition for a writ of certiorari seeking review of the same court of appeals' decision will be filed by the Solicitor General on behalf of the Federal Energy Regulatory Commission. In the event that such a petition is filed, the Public Power Group would, for the reasons set forth in this brief, urge that it, too, be granted.

Amicus Brief

7

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MOTION OF THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, PACIFIC GAS AND ELECTRIC COMPANY, SOUTHERN CALIFORNIA GAS COMPANY, AND SAN DIEGO GAS AND ELECTRIC COMPANY FOR LEAVE TO FILE BRIEF AMICI CURIAE

AND

BRIEF AMICI CURIAE IN SUPPORT OF PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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The Public Utilities Commission of the State of California (CPUC), Pacific Gas and Electric Company (PGandE), Southern California Gas Company (SoCal Gas), and San Diego Gas and Electric Company (San Diego) respectfully move this Court, pursuant to Rule 36.1, for leave to file the accompanying amici curiae brief. This motion is necessary because some of the parties to the proceeding before the United States Court of Appeals for the Fifth Circuit refused to consent to the filing of an amici curiae brief.

The CPUC is an administrative agency established under the Constitution and laws of the State of California. Among its duties, it exercises general regulatory jurisdiction over natural gas distribution companies within the State of California, including approval of service and rates and charges of these companies. The CPUC is obligated to protect the people of the State of California, who are customers of the gas companies, and is authorized to represent them in proceedings of this nature.

PGandE and SoCal Gas are natural gas transmission and distribution companies incorporated under the laws of the State of California. PGandE distributes gas and electricity throughout the northern and central parts of California which include approximately 8.7 million people and 3.0 million gas customers. SoCal Gas purchases, distributes and sells natural gas in the central and southern parts of California which include approximately 12.4 million people and 3.8 million gas customers.

San Diego is incorporated under the laws of the State of California. In addition to its service of electricity, San Diego distributes gas for consumption by retail purchasers in the City of San Diego, California, and in various cities and communities in San Diego County. San Diego obtains all of its natural gas from SoCal Gas.

Overall, the residential, commercial and industrial consumers within the State of California purchase more natural gas than consumers in any other state. Approximately 90 percent of the natural gas burned in California comes from sources outside the state. Over half of that supply comes from El Paso Natural Gas Company (El Paso), an

interstate natural gas pipeline regulated by the Federal Energy Regulatory Commission (FERC). SoCal Gas and PGandE purchase approximately 80 percent of the natural gas which El Paso transports through its interstate pipeline system. The volume of purchases by SoCal Gas and PGandE make them El Paso's two largest customers.

El Paso currently sells in excess of three billion cubic feet of natural gas per day to its customers or over one trillion cubic feet a year. A substantial portion of El Paso's gas supplies are the result of an extensive in-house drilling and production program, which has been ongoing for over thirty years. Approximately 80 percent of El Paso's in-house production of gas has been priced on a cost-of-service basis with the approval of the Federal Power Commission and its successor, the FERC. Thus, for over 30 years, the purchasers and consumers of El Paso's natural gas in California have, through cost-of-service pricing, paid for El Paso's risks and costs of production of said gas, plus a reasonable return on the investment in production.

The CPUC, PGandE, SoCal Gas and San Diego are therefore vitally interested in the scope of the FERC's authority in the pricing of pipeline-produced gas and the outcome of this litigation. The decision of the United States Court of Appeals for the Fifth Circuit under review could permit El Paso to raise the price it charges its customers to the Natural Gas Policy Act of 1978 (NGPA) maximum lawful ceiling prices for its pipeline-produced gas. Since El Paso has no incentive to bargain with itself in an effort to keep prices at reasonable levels, El Paso can be expected to and is attempting to increase its price to the maximum

lawful price, thereby increasing the price of El Paso's gas to California purchasers and consumers by hundreds of millions of dollars annually.

We recognize that some of the matters raised in the accompanying amici curiae brief may be addressed in the petitions for a writ of certiorari on file or to be filed with this Court. However, due to the importance of the issues raised and the magnitude of the injustice created by the Court of Appeals decision, the CPUC, PGandE, SoCal Gas and San Diego seek leave to file the attached brief to set forth our views on the issues presented in this proceeding, to inform this Court of the gross inequities which would result from the Court of Appeals decision and to establish that the Court of Appeals views are inconsistent with the mandate of the NGPA.

WHEREFORE, the CPUC, PGandE, SoCal Gas and San Diego respectfully move the Court for leave to file the accompanying amici curiae brief in these proceedings.

Dated: May 7, 1982.

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TABLE OF CONTENTS

	Page
Table of Authorities	ii
Interest	2
Summary of Argument	3
Argument	4
I	
The Court of Appeals decision conflicts with fundamental principles of ratemaking and equity	4
II	
The Court of Appeals has impermissibly directed FERC to perform its discretionary duties in a way which is inconsistent with the NGPA	8
Conclusion	12

TABLE OF AUTHORITIES

Cases

	Page
Batterton v. Francis, 432 U.S. 416 (1977)	11
Canadian River Gas Co., et al., 3 F.P.C. 32 (1942), aff'd sub nom., Colorado Interstate Gas Co. v. FPC, 324 U.S. 581 (1945)	5
Columbia Gas Development Corp. v. FERC, 651 F.2d 1146 (5th Cir. 1981)	5
Democratic Cent. Com. of D.C. v. Washington M.A.T. Com'n., 485 F.2d 786 (D.C. Cir. 1973), cert. den., 415 U.S. 935 (1974)	6
Montana Power Co. v. Federal Energy Reg. Com'n, 599 F.2 . 295 (9th Cir. 1979)	6
Pennzoil Co. v. Public Service Commission of West Virginia, Case No. 80-175-G-42T (January 19, 1982) cert. pending, Pennzoil Co. v. Public Service Commission of West Virginia, Supreme Court Docket No. 81-1672 (filed March 10, 1982)	10
Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738 (1969) mod. 42 F.P.C. 1089, aff'd sub nom., City of Chicago, Ill. v. FPC, 458 F.2d 731 (D.C. Cir. 1971), cert. den., 405 U.S. 1074 (1972)	6
Tenneco Oil Co. v. Federal Energy Administration, 613 F.2d 298 (Temp. Emer. Ct. App. 1979)	10

FERC Orders

Order No. 58, Docket No. RM80-7 (issued November 14, 1979)	2, 4, 5, 6, 9, 11
Order No. 98, Docket No. RM80-6 (issued August 4, 1980)	2, 4, 5, 6, 11
Order No. 102, Docket Nos. RM80-7 and RM80-6 (issued October 3, 1980)	6, 9

Table of Authorities

Statutes

	Page
Natural Gas Act, 15 U.S.C. § 717 et seq.	2, 5
Natural Gas Policy Act of 1978, 15 U.S.C. § 3301 et seq.	Passum
Section 2 (20), 15 U.S.C. § 3301 (20)	8
Section 2 (21)A, 15 U.S.C. § 3301 (21)A	8
Section 2 (21)B, 15 U.S.C. § 3301 (21)B	9
Section 101(b)(9), 15 U.S.C. § 3311(b)(9)	7
Section 104, 15 U.S.C. § 3314	9
Section 315, 15 U.S.C. § 3375	9
Section 501(b), 15 U.S.C. § 3411(b)	11
Section 601(b)(1)(E), 15 U.S.C. § 3431(b)(1)(E)	7

Miscellaneous

H.R. Conf. Rep. No. 95-1752, 95th Cong., 2nd Sess. 116 reprinted in [1978] U.S. Code Cong. & Ad. News 8983, 9033	11

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Petitioners,

VS.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

BRIEF AMICI CURIAE OF THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, PACIFIC GAS AND ELECTRIC COMPANY, SOUTHERN CALIFORNIA GAS COMPANY, AND SAN DIEGO GAS AND ELECTRIC COMPANY IN SUPPORT OF PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The Public Utilities Commission of the State of California, Pacific Gas and Electric Company, Southern California Gas Company, and San Diego Gas and Electric Company (hereinafter "California") herewith submit our brief, amici curiae, in support of the petitions for a writ of certiorari filed by the Public Service Commission of the State of New York (No. 81-1889), Arizona Electric Power Cooperative, Inc. (No. 81-1958), and the State of Michigan

(No. 81-.....). For the reasons set forth below, the United States Court of Appeals for the Fifth Circuit erred in vacating Orders Nos. 58 and 98 of the Federal Energy Regulatory Commission (FERC) in the decision reported below at *Mid-Louisiana Gas Company et al. v. FERC*, 664 F.2d 530 (1981). The orders vacated by the Court of Appeals:

1. Continued cost-of-service pricing for commingled pipeline-produced natural gas produced from older wells and leases and for commingled pipeline-produced gas sold pursuant to Federal Power Commission (FPC) or FERC orders specifically authorizing such pricing;

2. Refused to redefine the phrase "transfer for value" in a way that is inconsistent with the terms of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. § 3301 *et seq.*; and

3. Coordinated the underlying policies of the Natural Gas Act (NGA), 15 U.S.C. § 717 *et seq.*, and the NGPA by continuing NGA principles of ratemaking for older wells and leases and other wells previously priced on a cost-of-service basis, and by allowing NGPA maximum ceiling prices as an incentive for pipeline-produced gas from newer wells and leases.

INTEREST

As set forth in the accompanying motion for leave to file brief amici curiae, which is incorporated herein by reference, California has a vital interest in the outcome of this litigation since we represent the largest group of natural

gas consumers in any state in the United States. The Fifth Circuit's decision, if permitted to stand, may result in an additional increase of over two hundred million dollars annually in the price of natural gas to California purchasers and consumers.

Consequently, the purchasers and ultimate consumers of natural gas in California and throughout the United States will be adversely and severely affected unless this Court grants certiorari and reverses the decision of the court below.

SUMMARY OF ARGUMENT

The Court of Appeals decision, disregarding the terms of the NGPA and the expertise of the FERC, will permit drastic increases in the price of natural gas which had been priced on a cost-of-service basis. The decision ignores fundamental ratemaking principles and is grossly inequitable since purchasers and consumers of said natural gas have already substantially paid for its cost of production.

The court below erred in its determination that a first sale pursuant to the NGPA occurs when a pipeline producer merely transfers from its production division to its pipeline division quantities of natural gas. In fact no first sale takes place.

The court's error results in defining the terms "sale" and "transfer for value" in a way that is inconsistent with the NGPA, the long history of the regulation of pipeline producers as distinct from independent producers, the common meaning of these terms and the opinion of the Temporary Emergency Court of Appeals, and directly conflicts with

the opinion of the Supreme Court of Appeals for the State of West Virginia.

ARGUMENT

I

THE COURT OF APPEALS DECISION CONFLICTS WITH FUNDAMENTAL PRINCIPLES OF RATE-MAKING AND EQUITY

With complete disregard for the FERC's expertise in pipeline regulation, the Court below vacated the FERC's Orders Nos. 58 and 98, while deciding that all sales of pipeline-produced gas must be treated as first sales and thus eligible for NGPA maximum lawful ceiling prices. The Court of Appeals decision may allow pipelines, for the first time, to arbitrarily increase the price payable, without the constraints of arm's length bargaining, to the NGPA ceiling prices for natural gas which they produce, that had been previously priced on a much lower cost-of-service basis. The Fifth Circuit achieved this monumental result by erroneously concluding that a bookkeeping transfer from a pipeline's production division to its transportation division constitutes a sale or other transfer for value (App. A-11).[1]

In promulgating rules concerning first sales, the FERC recognized that once pipeline-produced gas is commingled with other natural gas, the sale is no longer attributable to the pipeline's own production. Therefore, in Order No. 58,

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[1]Appendix references refer to the Appendix filed herein in conjunction with the petition for a writ of certiorari of the Public Service Commission of the State of New York (No. 81-1889).

the FERC declared that the sale of pipeline-produced gas would only be treated as a first sale under the NGPA if the gas is sold at the wellhead in an offsystem sale or if the sale is otherwise comprised exclusively of the pipeline's own produced gas. (App. B-2)

In Order No. 98, the FERC attempted to coordinate the underlying policies of the NGA and NGPA by allowing NGPA maximum ceiling prices as an incentive for pipeline-produced gas from newer wells and leases, while continuing cost-of-service pricing for gas from wells drilled prior to January 1, 1973 on leases acquired prior to October 8, 1969, or gas which has always been priced on a cost-of-service basis (i.e., due to settlement agreements or special circumstances). (App. B-25-27).[2]

The Fifth Circuit's decision vacating the FERC's Orders Nos. 58 and 98 results in a drastic change in the pricing of old, flowing gas, and conflicts with 40 years of pipeline production regulation as well as fundamental principles of ratemaking and equity. Ever since the NGA was enacted in 1938, the costs incurred by pipelines, along with reasonable rates of return, have been included in their cost-of-service prices to their customers. *Canadian River Gas Co., et al.*, 3 F.P.C. 32 (1942), *aff'd sub nom. Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581 (1945). Thus all of the costs of production and risks incurred in the search for gas by the

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[2]FERC's approach is consistent with the overall purposes of the NGPA to provide for incentive pricing for new gas and price controls on intrastate gas but to maintain NGA price controls on old gas to prevent unnecessary price increases. *Columbia Gas Co. v. Federal Energy Com'n*, 651 F.2d 1146, 1160 (5th Cir. 1981).

pipelines (including unsuccessful efforts) have been shifted from the stockholders to the customers of the pipeline. *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738, 756-7 (1969) *mod.* 42 F.P.C. 1089, *aff'd sub nom. City of Chicago, Ill. v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. den.*, 405 U.S. 1074 (1972). The FERC recognized the gross unfairness of changing pricing policy for gas historically priced on a cost-of-service basis and in Order No. 102 declared that "to vary this policy now would deprive these purchasers of price benefits they should receive in exchange for assuming the risk of a pipeline's production ventures." (App. B-73).

In Orders Nos. 58 and 98, the FERC attempted to maintain the most fundamental principle of ratemaking—that he who bears the financial burden of particular utility activity should also reap the benefits resulting therefrom. *Democratic Cent. Com. of D.C. v. Washington M.A.T. Com'n*, 485 F.2d 786, 806 (D.C. Cir. 1973), *cert. den.*, 415 U.S. 935 (1974). Indeed, the very task of regulation is to prevent consumers from bearing more than their fair share of the costs of utility service when competitive forces do not otherwise protect them. *Montana Power Co. v. Federal Energy Reg. Com'n.*, 599 F.2d 295, 299-300 (9th Cir. 1979).

The decision of the court below ignores the history and equities of cost-of-service pricing for pipeline-produced gas, ignores the delicate balance Congress attempted to strike between consumer pricing concerns and the need to provide pricing incentives to stimulate production of new gas supplies, and contradicts fundamental principles of rate-

making. Unlike their dealings with independent producers, pipelines have no incentive to bargain for their own production, since the higher the price paid for pipeline production, the greater the pipeline's profitability. Abandonment of cost-of-service pricing may result in a tremendous windfall to pipeline producers, who did not assume the risk or pay for costs of production of cost-of-service gas, in contrast to independent natural gas producers who did.

The losers will be natural gas consumers who agreed to cost-of-service pricing, even though it often meant higher prices at that time. With the shift ordered by the Fifth Circuit, consumers will have paid higher prices for the gas under cost-of-service pricing in the early years, plus the applicable NGPA maximum lawful price in later years. This result was not mandated by Congress, which restricted independent gas producers to the lower of the contract price or the NGPA maximum ceiling prices, 15 U.S.C. § 3311(b)(9). Pipelines are not so restricted because they have no incentive for arm's length bargaining and generally have no contracts for their own production.[3] Congress could not and did not intend the result reached by the court below.

In California alone, where gas purchasers and consumers have already paid for a substantial portion of the costs of

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[3]Congress restricted the price of affiliates' sales to pipelines to comparable sales made by unaffiliated companies. 15 U.S.C. § 3431 (b)(1)(E). However, Congress did not provide for such a restriction on the "price" a pipeline production division "charged" its transportation division because Congress apparently did not consider such transfers to be first sales.

production and risks of its major supplier, El Paso Natural Gas Company, for over 30 years, the decision of the court below could annually increase natural gas prices by over $200 million. The overall national impact of this decision, if allowed to stand, could be an astronomical windfall to pipeline producers.

II

THE COURT OF APPEALS HAS IMPERMISSIBLY DIRECTED FERC TO PERFORM ITS DISCRETIONARY DUTIES IN A WAY WHICH IS INCONSISTENT WITH THE NGPA

The NGPA establishes maximum ceiling prices for first sales of natural gas. The "first sale" treatment of natural gas requires that an actual sale take place. 15 U.S.C. § 3301(21)(A). The NGPA defines the term "sale" as "any sale, exchange or other transfer for value." 15 U.S.C. § 3301(20).

The court below erred in its determination that a first sale pursuant to the NGPA occurs when a pipeline producer merely transfers from its production division to its pipeline division quantities of natural gas. In fact no first sale takes place. While the court looked at the face of the legislation to determine its intent, it failed to give proper weight to the statutory definition of the term "sale". A first sale cannot occur in the absence of a transfer of title for value. Since no transfer of title for value occurs between a pipeline's own divisions, such transactions are not first sales. Moreover the subsequent sale of the gas in a commingled flow to a downstream customer of the pipeline

also does not constitute a first sale for the purposes of the NGPA because of the restriction, properly recognized by the court below, of 15 U.S.C. § 3301(21)(B), which "operates to eliminate this possibility by denying 'first sale' status to the downstream sale". (App. A-8) The court erred in concluding in effect that a first sale had to occur somewhere as to pipeline production. Such is not the case. The term "first sale" is a NGPA term of art having no applicability to the pipeline producer's transfer of gas from its production to its pipeline division. Instead, as the FERC recognized, NGA pricing principles of pipeline production are still applicable.

The FERC, after considering extensive comments, had twice rejected such a redefinition of intracorporate transfers. In Order No. 58, the FERC refused to treat such bookkeeping entries as sales, noting that such fiction would extend NGPA first sale jurisdiction to industrial corporations which consume their own natural gas. (App. B-5-6). In Order No. 102, upon rehearing of Order No. 58, the FERC found the intracorporate transactions to be inconsistent with the term "sale" since there had been no contracts, certificate authorizations or arm's length bargaining for the gas, and therefore such an interpretation would contradict the reference in Section 104 of the NGPA to sales of natural gas prior to the NGPA, 15 U.S.C. § 3314, and to the reference in Section 315 of the NGPA to contracts, bona fide offers, and right of first refusal. 15 U.S.C. § 3375 (App. B-66).

The court's decision which orders the FERC to treat such intracorporate transactions as first sales directly con-

flicts with the decision of the Supreme Court of Appeals for the State of West Virginia, which, by denying Pennzoil's petition for an appeal of the order of the Public Service Commission of West Virginia, correctly concluded that the FERC's position is proper. (See *Pennzoil Company v. Public Service Commission of West Virginia*, Case No. 80-175-G-42T (January 19, 1982), *cert. pending, Pennzoil Co. v. Public Service Commission of West Virginia*, No. 81-1672 (filed March 10, 1982)).

The Fifth Circuit has directed the FERC to treat intracorporate transfers as sales, whereas another Court of Appeals has held that the Federal Energy Administration could not treat intracorporate transfers as sales because such transfers are inconsistent with the word "sales". In *Tenneco Oil Co. v. Federal Energy Administration*, 613 F.2d 298, 302 (Temp. Emer. Ct. App. 1979), the court declared:

> "The first principle of regulatory construction is that regulatory terms must be interpreted according to their commonly understood definitions in the absence of a specific regulatory definition. *Burnes v. Alcala*, 420 U.S. 575 (1975); *Addison v. Holly Hill Fruit Products*, 322 U.S. 607 (1944). The commonly understood meaning of a 'sale' is a *transfer of title* in return for valuable consideration. *Commisisoner of Internal Revenue v. Brown*, 380 U.S. 563 (1965). The FEA cites no cases that are to the contrary. To hold that a 'sale' may occur simply in the receipt of value from property would be to rob from the term any legal or economic significance. See *Mobil Oil Corp. v. Federal Power Commission*, 463 F.2d 256, 262-63 (D.C. Cir.) *cert. denied*, 406 U.S. 976 (1972)."

Assuming *arguendo* that the FERC could redefine "transfer for value" or "sale" so as to include intracorporate transactions, yet not be inconsistent with the NGPA, the FERC is not required to do so. Congress specifically delegated the authority to define terms to the FERC, 15 U.S.C. § 3411(b), not to the courts.

The court below erroneously refers to the FERC's Orders Nos. 58 and 98 as interpretative regulations rather than substantive regulations. As the NGPA conference report makes clear, however, Congress specifically delegated to the FERC the authority to define terms such as "transfer for value." H.R. CONF. REP. NO. 95-1752, 95th Cong., 2nd Sess. 116 *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 8983, 9033. Therefore, the FERC's regulations concerning the meaning of "sales" and "transfers for value" as used in the NGPA are substantive regulations and the Court of Appeals "is not free to set aside those regulations simply because it would have interpreted the statute in a different manner." *Batterton v. Francis*, 432 U.S. 416, 425 (1977).

CONCLUSION

For the above-mentioned reasons, the petitions for a writ of certiorari should be granted.

Dated: May 7, 1982.

Respectfully submitted,

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Amicus Brief

8

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NO. 81-1889

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

Petitioner,

v.

MID-LOUISIANA GAS COMPANY, et al.,

Respondents.

BRIEF AS AMICUS CURIAE OF THE STATE OF WEST VIRGINIA IN SUPPORT OF THE PETITION OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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May 12, 1982

TABLE OF CONTENTS

Page

THE INTEREST OF THE AMICUS CURIAE.....1

ARGUMENT 5

SUMMARY OF ARGUMENT.....6

CONCLUSION.....7

INTEREST OF THE STATE OF WEST VIRGINIA AS AN AMICUS CURIAE

The State of West Virginia through its various governmental agencies is a consumer of natural gas. Additionally, there are approximately forty-six (46) natural gas utilities in the State which sell natural gas on a retail basis to numerous residential, industrial and commercial customers. Total demand for natural gas in 1981 by West Virginia consumers was approximately 150 billion cubic feet. Certainly, the general welfare of its citizenry is of concern to the State.

Approximately 75% of the natural gas sales to consumers in the State are made by Columbia Gas of West Virginia and the Hope Division of Consolidated Natural Gas Corporation.[1] All of Hope Division's gas is supplied by Consolidated Natural Gas Corporation, an interstate pipeline. Approximately 93% of Columbia Gas of West Virginia's gas supply comes from its affiliate Columbia Gas Transmission Corporation, an interstate pipeline.[2] These two interstate pipelines and other interstate pipelines supply gas to the remaining gas utilities in the State. Clearly, most of the gas sold in the State is furnished by interstate pipelines whose rates and charges for gas supplied to local utilities are established by the Federal Energy Regulatory Commission. Consequently, to the ex-

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[1]Report to the West Virginia Legislature by the West Virginia Public Service Commission, *Supply-Demand Forecast for Gas Utilities*, 1981-1990, February 11, 1981.

[2]1981 Annual Report of Columbia Gas of West Virginia to the Public Service Commission of West Virginia.

tent that the Court's opinion in *Mid-Louisiana Gas Company* v. *FERC*, 664 F.2d 530 (1981), reh'g denied, _____ F.2d _____ (5th Cir. 1982) remains intact, the FERC's past policy regarding cost of service treatment of interstate pipeline production remains vacated, the resulting increased gas costs will be flowed through to consumers by the FERC-approved purchased gas adjustment provisions of the particular interstate pipelines without the possibility of review by this State as a result of the Supremacy Clause of the United States Constitution.

It is not possible to quantify the precise impact of the Court's decision; however, even a conservative, rough estimate indicates that the impact will result in an annual increase in natural gas costs of several million dollars to West Virginia consumers which cannot be considered *de minimis*.[3] As indicated in the Petition for a Writ of Certiorari of the Public Service Commission of the State of New York[4], Columbia Gas Transmission Corp. (TCo) has provided evidence that 76.43% or 30,835,900 Mcf of its production for the twelve months ending February 28, 1982, was priced by the FERC on a cost of service basis. See Exhibit 52, *Columbia Gas Transmission Corp.*, FERC

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[3]The information needed to compute the impact of *Mid-Louisiana* lies with the interstate pipelines and is not currently available except on a piecemeal basis. Contributing to the problem is the fact that interstate pipelines purchase some of their gas supply from other interstate pipelines. For example, substantial quantities of gas which make up the total gas supply of Columbia Gas Transmission Corporation and Consolidated Gas Supply Corporation are purchased from other interstate pipelines — Panhandle Eastern Pipeline Co., Tennessee Gas Pipeline Co., Texas Eastern Transmission Corp., Texas Gas Transmission Corp., and Transcontinental Gas Pipeline which presumably have cost of service production of their own which will be subject to NGPA repricing and which will result in increased costs to Columbia and Consolidated and eventually their customers. Thus, *Mid-Louisiana* will have a ripple effect.

[4]New York's Petition, p. 18.

Docket No. TA81-1-21 *et al.* In 1981, approximately 5.5% of TCo's total sales were to Columbia Gas of West Virginia[5]. If New York's conservative estimates that only half of that production will qualify for Section 108 prices under the Natural Gas Policy Act of 1978 and that this will result in an increase in total annual gas costs of $38,390,695 are used for illustrating the impact of the Court's decision[6], 5.5% of those costs or approximately $2,111,488 will be borne by West Virginia consumers.

Recently, Consolidated Gas Supply Corporation filed a notice of proposed changes in its FERC Gas Tariff to reflect the partial implementation of *Mid-Louisiana.*[7] The proposed change would increase FERC jurisdictional rates by $25,186,808 on an annual basis. The FERC non-jurisdictional increase, which is solely attributable to the Hope Division's sales to West Virginia consumers, is $2,033,876 which will be passed through to West Virginia consumers.[8] Consolidated expressly reserved the right to collect NGPA rates retroactively to December 1, 1978.[9]

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[5]1981 Annual Reports of Columbia Gas Transmission Corporation and Columbia Gas of West Virginia.

[6]New York's estimate appears on pages 18-19 of its Petition. The West Virginia Public Service Commission does not disagree with the figure but views it as conservative.

[7]"Notice of Proposed Changes in FERC Gas Tariff," 47 Federal Register 17619, April 23, 1982.

[8]Consolidated Gas Supply Corporation, FERC Docket No. RP82-64-000, Schedule 1 attached to revised tariff sheets.

[9]Consolidated Gas Supply Corporation, FERC Docket No. RP82-64-000, letter from John T. Stough, Jr., Esquire to Mr. Plumb, April 1, 1982, p. 2.

Therefore, West Virginia consumers of two local utilities, Columbia Gas of West Virginia and the Hope Division of Consolidated Natural Gas Corporation, face a minimum annual increase in purchased gas costs of $4,145,364 as a direct result of the Court's decision in *Mid-Louisiana*. It should be reemphasized that this increase does not include anticipated price increases to Columbia Gas Transmission Corporation and Consolidated Gas Supply Corporation as a result of the repricing of cost of service production by other interstate pipelines. Furthermore, it does not consider sales by these two interstate pipelines and other interstate pipelines to other gas utilities in the State. Over this entire analysis, is the specter of the retroactive application of the *Mid-Louisiana* decision to the December, 1978 effective date of the Natural Gas Policy Act.

Clearly, West Virginia consumers face the imminent burden of a multi-million dollar increase in annual natural gas costs as a result of the Court's decision in *Mid-Louisiana*.

ARGUMENT

The State of West Virginia concurs with and adopts the Question Presented, the Statement of the Case, and the Reasons for Granting the Writ as set forth in the "Petition For a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit" filed before this Court by the Public Service Commission of the State of New York.

SUMMARY OF ARGUMENT

Since the State of West Virginia has adopted the argument of the Public Service Commission of New York as hereinbefore indicated, it believes that the Court's decision in *Mid-Louisiana* is erroneous. If unreviewed by this Court, the decision will result in West Virginia consumers contributing millions of dollars in unwarranted windfall profits to interstate pipelines.

CONCLUSION

Due to the legal questions of first impression, the erroneous resolution of those questions by the Court in *Mid-Louisiana,* and the substantial financial impact on West Virginia consumers, the State of West Virginia urges this Court to grant the Writ of Certiorari requested in the Petition of the Public Service Commission of New York.

Respectfully submitted,

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Respondent's Reply Brief

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Nos. 81-1889, 81-1958 and 81-2042

In the
SUPREME COURT OF THE UNITED STATES
October Term, 1981

THE PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK,
ARIZONA ELECTRIC POWER
COOPERATIVE, INC.
AND STATE OF MICHIGAN,
Petitioners,

v.

MID-LOUISIANA GAS COMPANY, et al.,
Respondents.

ON PETITIONS FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

RESPONSE IN OPPOSITION AND OBJECTION OF COLORADO INTERSTATE GAS COMPANY TO MOTION OF THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, PACIFIC GAS AND ELECTRIC COMPANY, SOUTHERN CALIFORNIA GAS COMPANY, AND SAN DIEGO GAS AND ELECTRIC COMPANY FOR LEAVE TO FILE BRIEF AMICI CURIAE

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May 19, 1982

TABLE OF CONTENTS

Listing of Affiliates Pursuant to Rule 28.1 i

Response of Colorado Interstate Gas Company 1

TABLE OF AUTHORITIES

Judicial Decisions:

Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380 (1947) 4

Mid-Louisiana Gas Company, et al. v. Federal Energy Regulatory Commission, 664 F.2d 530 (5th Cir., 1981) 3

Statutes

44 U.S.C. § 1507 (1976) 4

Other Authorities

U.S. Sup. Ct. R. 36.3 2

U.S. Sup. Ct. R. 42.4 2

LISTING OF AFFILIATES PURSUANT TO RULE 28.1

Colorado Interstate Gas Company, one of a number of parties below listed in the petitions for a writ of certiorari by the Public Service Commission of the State of New York in No. 81-1889, Arizona Electric Power Cooperative, Inc., in No. 81-1958, and the State of Michigan in No. 81-2042, is a wholly owned subsidiary of Colorado Interstate Corporation. Colorado Interstate Corporation is, in turn, a wholly owned subsidiary of The Coastal Corporation. The remaining subsidiaries of The Coastal Corporation and affiliates of Colorado Interstate Gas Company are as follows:

Coastal Refining Company, Coastal States Petroleum Company, Coastal States Crude Gathering Company, Coastal States Marketing, Inc.,

CIC Industries, Inc., Derby Refining Company, Pacific Refining Company, Western Fuel Oil Company, Wycon Chemical Company, Coastal Energy Corporation, Coastal Refinery Marketing B.V., Coastal Ventures, Inc., Raffinerie Belge de Petroles S.A. (Belgische Petroleum Raffinaderij N.V.), Coastal Management Services (Singapore) Pte. Ltd., Coastal States Energy Company, Alaska Petroleum Company, Freeburn Corporation, McCoy-Caney Coal Company, Southern Utah Fuel Company, Utah Fuel Company, Coastal States Management Corporation, Coastal States Trading, Inc., CIG Exploration, Inc., Cosbel Petroleum Corporation, The Belcher Company of New York, Inc., Belcher New England, Inc., Belcher New Jersey, Inc. Belcher Oil Company, Belcher Towing Company, Manatee

Towing Company, Belcher Terminals, Inc., Belcher Oil Company of Pensacola, The Belcher Company of Alabama, Inc., The Belcher Company of Georgia, Inc., The Belcher Company of Tennessee, Inc., The Belcher Company of Texas, Inc., Coscol Petroleum Corporation, Costa Petro, Coastal Libya, Inc., Coastal Petroleum (Far East) Pte.Ltd., Coscol Marine Corporation, Coskan Shipping Co., Inc., Holborn Oil Company Limited, Holborn Petroleum S.A., Union Oil Trading & Shipping Limited, Bunyan Charterers Ltd., Coastal States Europe Limited, Pomona Shiping Company Limited, Succula Limited, Coastal States Exploration Services Limited, Coastal States Petroleum (U.K.) Limited, Coastal States Trading (U.K.) Limited, Woodstock

Shipping Company Limited, Subtype Limited, Holborn-Pomona Petroleum Limited, Holborn Oil Trading Limited, Coastal (Bermuda) Limited, Geogas Enterprise S.A., Sequoia Tankers, Inc., Stonehurst Limited, Texas Tank Ship Agency, Inc., Texcol Gas Services, Inc., Coastal Oil & Gas Corporation, Border Exploration Company, Coastal Congo Exploration Limited, Coastal Indonesia, Inc., Coastal Libya Exploration Limited, Coastal Papua New Guinea Exploration, Inc., Coastal Uranium, Inc., Syrian American Oil Corporation (Texas), Western Enterprises, Inc., CLU Enterprises, Inc., Coastal Christi, Inc., Coastal Hercules, Inc., Coastal Capital Corporation, Coastal Finance Corporation, Coastal Overseas Finance Ltd., Coastal Netherlands

Financial B.V., Coastal Financial B.V., Coastal Financial Antilles, N.V., Coastal Offshore Insurance, Ltd., Colbourne Insurance Company Limited, Coastal Limited Ventures, Inc., Coastal 1981 Development Program, Ltd., Coastal 1982 Drilling Program, Ltd., CIG Gas Supply Company, Wyoming Gas Supply, Inc., Coastal Coal Sales Company, Overthrust Pipeline Company, Wyoming Interstate Company, Ltd., Petroles D'Outre Mer S.A., and Jayhawk Pipeline Corporation.

Nos. 81-1889, 81-1958 and 81-2042

In the
SUPREME COURT OF THE UNITED STATES
October Term, 1981

THE PUBLIC SERVICE COMMISSION
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Colorado Interstate Gas Company (hereinafter "CIG"), pursuant to Rules

36.3 and 42.4 of the Rules of the Supreme Court of the United States, respectfully submits this response in opposition and objection to the Motion of the Public Utilities Commission of the State of California, Pacific Gas and Electric Company, Southern California Gas Company and San Diego Gas and Electric Company (hereinafter "California Movants") for leave to file brief amici curiae. The motion is dated May 7, 1982 and was received by CIG on May 10, 1982. CIG was a participant in the Federal Energy Regulatory Commission (hereinafter "Commission") proceedings which gave rise to these petitions for a writ of certiorari and was an intervenor in the proceedings below before the United States Court of Appeals for the Fifth Circuit. CIG

supports the decision below1/ and will show in its brief in opposition to the petitions herein that no compelling reason has been demonstrated for the issuance of a writ of certiorari in this matter.

The subject motion for leave to file brief amici curiae should be denied.

All of the California Movants had notice of the originating Commission

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1/ Mid-Louisiana Gas Company, et al. v. Federal Energy Regulatory Commission, 664 F.2d 530 (5th Cir., 1981).

proceedings.2/ Additionally, the California Movants chose, for whatever reason, not to file a motion for leave to intervene in the proceedings below before the United States Court of Appeals for the Fifth Circuit. No justification is shown by the California Movants as to why they could not have protected their asserted interests by being parties below and before this Court.

2/ The Commission proceedings at Docket No. RM80-6 began with a Notice of Proposed Rulemaking issued November 14, 1979 which was published in the Federal Register (44 Fed. Reg. 66612, Nov. 20, 1979). The Commission proceedings at Docket No. RM80-7 resulted in the promulgation of final regulations which were originally proposed for comment in November of 1978 and issued as interim regulations on December 1, 1979 (43 Fed. Reg. 56448, December 1, 1978). Publication of these documents in the Federal Register is legally deemed to be notice to all interested parties. 44 U.S.C. §1507 (1976). See also Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380 (1947).

Furthermore, the California Movants do not reveal in their motion or the "Brief Amici Curiae . . ." appended thereto any substantial reason why their participation will uniquely aid the Court in disposing of these petitions for a writ of certiorari. In fact, the California Movants recognize that their arguments in support of the petitions may be redundant and cummulative when they state as follows:

> We recognize that some of the matters raised in the accompanying amicus curiae brief may be addressed in the petitions for a writ of certiorari on file or to be filed with this Court. (Motion, page 4).

In conclusion, the subject motion should be denied since it fails to demonstrate sufficient grounds for the relief sought.

Respectfully submitted,

COLORADO INTERSTATE GAS COMPANY

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Dated: May 19, 1982

Respondent's Reply Brief

2

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No. 81-1889

In the
SUPREME COURT OF THE UNITED STATES
October Term, 1981

THE PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, et al.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

RESPONSE IN OPPOSITION AND OBJECTION OF COLORADO INTERSTATE GAS COMPANY TO MOTIONS OF THE ASSOCIATED GAS DISTRIBUTORS AND THE STATE OF KANSAS AND THE KANSAS CORPORATION COMMISSION FOR LEAVE TO FILE BRIEFS AMICUS CURIAE

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TABLE OF CONTENTS

Listing of Affiliates Pursuant to Rule 28.1 i

Response and Objection 1

TABLE OF AUTHORITIES

Judicial Decisions:

Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380 (1947) 3

Mid-Louisiana Gas Company, et al. v. Federal Energy Regulatory Commission, 664 F.2d 530 (5th Cir., 1981) 2

Statutes

44 U.S.C. § 1507 (1976) 3

Other Authorities

U.S. Sup. Ct. R. 36.3 1

U.S. Sup. Ct. R. 42.4 1

LISTING OF AFFILIATES PURSUANT TO RULE 28.1

Colorado Interstate Gas Company (hereinafter "CIG"), a respondent in these cases, has previously filed herein the listing of affiliates required by Rule 28.1 of the Rules of the Supreme Court of the United States. That listing accompanied CIG's "Response in Opposition and Objection . . . to Motion of the Public Utilities Commission of the State of California, Pacific Gas and Electric Company, Southern California Gas Company, and San Diego Gas and Electric Company for Leave to File Brief Amici Curiae." Said "Response . . ." was filed on May 19, 1982, and no amendments to it are necessary to make it currently accurate.

No. 81-1889

In the
SUPREME COURT OF THE UNITED STATES
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THE PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK,
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MID-LOUISIANA GAS COMPANY, et al.,
Respondents.

RESPONSE IN OPPOSITION AND OBJECTION OF COLORADO INTERSTATE GAS COMPANY TO MOTIONS OF THE ASSOCIATED GAS DISTRIBUTORS AND THE STATE OF KANSAS AND THE KANSAS CORPORATION COMMISSION FOR LEAVE TO FILE BRIEFS AMICUS CURIAE

Colorado Interstate Gas Company (hereinafter "CIG"), pursuant to Rules 36.3 and 42.4 of the Rules of the Supreme Court of the United States, respectfully submits this response in opposition and objection to the motions of the Associated Gas Distributors (hereinafter "AGD") and the

State of Kansas and the Kansas Corporation Commission (hereinafter collectively referred to as "Kansas") for leave to file briefs amicus curiae in the subject docket. The AGD motion is dated May 11, 1982 and was received by CIG on May 14, 1982. The Kansas motion is undated and was received by CIG on May 17, 1982.

CIG was a participant in the Federal Energy Regulatory Commission (hereinafter "Commission") proceedings which gave rise to these petitions for a writ of certiorari and was an intervenor in the proceedings below before the United States Court of Appeals for the Fifth Circuit. CIG supports the decision below1/ and will show in its

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1/ Mid-Louisiana Gas Company, et al. v. Federal Energy Regulatory Commission, 664 F.2d 530 (5th Cir., 1981).

brief in opposition to the petitions herein that no compelling reason has been demonstrated for the issuance of a writ of certiorari in this matter.

AGD and Kansas had notice of the originating Commission proceedings.2/ The Kansas Corporation Commission, in fact, was an active participant in those proceedings (See Appendix B-28). For whatever reason,

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2/ The Commission proceedings at Docket No. RM80-6 began with a notice of Proposed Rulemaking issued November 14, 1979 which was published in the Federal Register (44 Fed. Reg. 66612, Nov. 20, 1979). The Commission proceedings at Docket No. RM80-7 resulted in the promulgation of final regulations which were originally proposed for comment in November of 1978 and issued as interim regulations on December 1, 1978 (43 Fed. Reg. 56448, December 1, 1978). Publication of these documents in the Federal Register is legally deemed to be notice to all interested parties. 44 U.S C. Sec. 1507 (1976). See also Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380 (1947).

Kansas and AGD chose not to file motions for leave to intervene in the proceedings below before the United States Court of Appeals for the Fifth Circuit. No justification is shown by them here as to why they could not have protected their asserted interests by being parties below and before this Court.

Furthermore, AGD and Kansas do not reveal in their motions or their briefs appended thereto any substantial reason why their participation will uniquely aid the Court in disposing of these petitions for a writ of certiorari. The motions and briefs of AGD and Kansas instead demonstrate that the arguments of AGD and Kansas in support of the Public Service Commission of the State of New York petition have already been presented by that petition and the related petitions for writ of certiorari filed by Arizona Electric Power

Cooperative, Inc. in No. 81-1958 and the State of Michigan in No. 81-2042.

In conclusion, the subject motions should be denied since they fail to demonstrate sufficient grounds for the relief sought.

Respectfully submitted,

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Dated: May 23, 1982

Respondent's Reply Brief

3

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Nos. 81-1889, 81-1958, 81-2042 and 82-19

In the
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THE PUBLIC SERVICE COMMISSION OF
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MID-LOUISIANA GAS COMPANY, et al.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

RESPONSE IN OPPOSITION AND OBJECTION OF COLORADO INTERSTATE GAS COMPANY TO MOTION OF EDMUND G. BROWN, JR., GOVERNOR OF CALIFORNIA, FOR LEAVE TO FILE BRIEF AMICUS CURIAE

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August 16, 1982

TABLE OF CONTENTS

	Page
Listing of Affiliates Pursuant to Rule 28.1	ii
Response and Objection	1

TABLE OF AUTHORITIES

Judicial Decisions:

Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380 (1947)	4
Mid-Louisiana Gas Company, et al. v. Federal Energy Regulatory Commission, 664 F.2d 530 (5th Cir., 1981)	2

Statutes:

44 U.S.C. § 1507 (1976)	4

Other Authorities:

U.S. Sup. Ct. R. 36.3	1,2
U.S. Sup. Ct. R. 42.4	1
U.S. Sup. Ct. R. 36.4	2

LISTING OF AFFILIATES PURSUANT TO RULE 28.1

Colorado Interstate Gas Company (hereinafter CIG), a respondent in these cases, has previously filed herein the listing of affiliates required by Rule 28.1 of the Rules of the Supreme Court of the United States. That listing accompanied CIG's "Brief in Opposition of Respondent Colorado Interstate Gas Company" to the Petition for a Writ of Certiorari filed by the Solicitor General of the United States on behalf of the Federal Energy Regulatory Commission in No. 82-19. Said "Brief in Opposition . . ." was filed on August 4, 1982, and no amendments to it are necessary to make it currently accurate.

Nos. 81-1889, 81-1958, 81-2042 and 82-19

In the
SUPREME COURT OF THE UNITED STATES
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THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, et al.,
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v.

MID-LOUISIANA GAS COMPANY, et al.
Respondents.

RESPONSE IN OPPOSITION AND OBJECTION OF COLORADO INTERSTATE GAS COMPANY TO MOTION OF EDMUND G. BROWN, JR., GOVERNOR OF CALIFORNIA, FOR LEAVE TO FILE BRIEF AMICUS CURIAE

Colorado Interstate Gas Company (hereinafter "CIG"), pursuant to Rules 36.3 and 42.4 of the Rules of the Supreme Court of the United States, respectfully submits this response in opposition and objection to the motion of Edmund G. Brown, Jr., Governor of California, (hereinafter "Governor Brown"), for leave to file brief amicus curiae in the subject dockets. Governor Brown's motion is dated August 3, 1982, and was received by CIG on August 6, 1982.

Governor Brown's motion to file this brief amicus curiae is necessary because a party to the case refused to consent to the filing of the brief1/, and he is not within the exception permitting such briefs to be filed without making a motion.2/

CIG was a participant in the Federal Energy Regulatory Commission (hereinafter "Commission") proceedings which gave rise to these petitions for writ of certiorari and was an intervenor in the proceedings below before the United States Court of Appeals for the Fifth Circuit. CIG supports the decision below3/ and has shown in its

---

1/ See Rule 36.3 of the Rules of the Supreme Court of the United States.

2/ See Rule 36.4 of the Rules of the Supreme Court of the United States.

3/ Mid-Louisiana Gas Company, et al. v. Federal Energy Regulatory Commission, 664 F.2d 530 (5th Cir., 1981).

briefs in opposition to the petitions herein that no compelling reason exists or has been demonstrated for the issuance of a writ of certiorari in this matter.4/

4/ On May 25, 1982, CIG filed its Brief in Opposition to the Petitions for Writ of Certiorari filed by Public Service Commission of the State of New York, No. 81-1889, Arizona Electric Power Cooperative, Inc., No. 81-1958, and The State of Michigan, No. 81-2042.

On August 4, 1982, CIG filed its Brief in Opposition to the Petition for Writ of Certiorari filed by the United States Solicitor General on behalf of the Federal Energy Regulatory Commission, No. 82-19.

Governor Brown had notice of the originating Commission proceedings.5/ Governor Brown did not file a petition to intervene in the Commission proceedings or in the proceedings below before the United States Court of Appeals for the Fifth Circuit. No justification is shown by Governor Brown as to why he could not have protected his asserted interest by being a

---

5/ The Commission proceedings at Docket No. RM80-6 began with a Notice of Proposed Rulemaking issued November 14, 1979 which was published in the Federal Register (44 Fed. Reg. 66612, Nov. 20, 1979). The Commission proceedings at Docket No. RM80-7 resulted in the promulgation of final regulations which were originally proposed for comment in November of 1978 and issued as interim regulations on December 1, 1979 (43 Fed. Reg. 56448, December 1, 1978). Publication of these documents in the Federal Register is legally deemed to be notice to all interested parties. 44 U.S.C. § 1507 (1976). See also Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380 (1947).

proper party below and before this Court. The California Public Utilities Commission in association with other major California energy utilities has, as the Governor's motion recites, filed a brief amicus curiae, and has similar, if not the same interests, which the Governor alleges support a grant of this motion.

Furthermore, Governor Brown does not demonstrate or reveal in his motion or brief appended thereto any substantial reason why his participation will uniquely aid the Court in disposing of these petitions for a writ of certiorari.

Governor Brown's motion and brief amicus curiae contain arguments already presented by the petitions for a writ of certiorari. He has not demonstrated any expertise on the issue presented for review which is not possessed by the

parties who have already filed petitions for a writ of certiorari.

In conclusion, the subject motion should be denied since it fails to demonstrate an interest or sufficient grounds for the relief sought.

Respectfully submitted,

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Dated: August 16, 1982

Respondent's Reply Brief

4

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Nos. 81-1889, 81-1958, 81-2042 and 82-19

In the
SUPREME COURT OF THE UNITED STATES
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THE STATE OF NEW YORK, et al.,
Petitioners,

v.

MID-LOUISIANA GAS COMPANY, et al.,
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ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
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RESPONSE IN OPPOSITION AND OBJECTION OF COLORADO INTERSTATE GAS COMPANY TO MOTION OF THE NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

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August 19, 1982

TABLE OF CONTENTS

	Page
Listing of Affiliates Pursuant to Rule 28.1	ii
Response and Objection	1

TABLE OF AUTHORITIES

Judicial Decisions:

Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380 (1947)	4
Mid-Louisiana Gas Company, et al. v. Federal Energy Regulatory Commission, 664 F.2d 530 (5th Cir., 1981) . . .	3

Statutes:

44 U.S.C. § 1507 (1976)	4

Other Authorities:

U.S. Sup. Ct. R. 36.3	1,2
U.S. Sup. Ct. R. 42.4	1
U.S. Sup. Ct. R. 36.4	2

LISTING OF AFFILIATES PURSUANT TO RULE 28.1

Colorado Interstate Gas Company (hereinafter CIG), a respondent in these cases, has previously filed herein the listing of affiliates required by Rule 28.1 of the Rules of the Supreme Court of the United States. That listing accompanied CIG's "Brief in Opposition of Respondent Colorado Interstate Gas Company" to the Petition for a Writ of Certiorari filed by the Solicitor General of the United States on behalf of the Federal Energy Regulatory Commission in No. 82-19. Said "Brief in Opposition . . ." was filed on August 4, 1982, and no amendments to it are necessary to make it currently accurate.

Nos. 81-1889, 81-1958, 81-2042 and 82-19

In the
SUPREME COURT OF THE UNITED STATES
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THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, et al.,
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MID-LOUISIANA GAS COMPANY, et al.,
Respondents.

RESPONSE IN OPPOSITION AND OBJECTION OF COLORADO INTERSTATE GAS COMPANY TO MOTION OF THE NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

Colorado Interstate Gas Company (hereinafter "CIG"), pursuant to Rules 36.3 and 42.4 of the Rules of the Supreme Court of the United States, respectfully submits this response in opposition and objection to the motion of the National Rural Electric Cooperative Association (hereinafter "NRECA") for leave to file brief amicus curiae in the subject dockets. NRECA's motion is dated August 4, 1982, and was received by CIG on August 9, 1982.

NRECA's motion to file this brief amicus curiae is necessary because a party to the case refused to consent to filing of the brief1/, and it is not within the exception permitting such briefs to be filed without making a motion.2/

CIG was a participant in the Federal Energy Regulatory Commission (hereinafter "Commission") proceedings which gave rise to these petitions for writ of certiorari and was an intervenor in the proceeding below before the United States Court of Appeals for the Fifth Circuit. CIG supports the

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1/ See Rule 36.3 of the Rules of the Supreme Court of the United States.

2/ See Rule 36.4 of the Rules of the Supreme Court of the United States. While NRECA states that it's motion to file brief amicus curiae is necessary because consent of certain respondents to file was not obtained (Motion, p. 2), NRECA incorrectly relies on Rule 36.4 of the Rules of the Supreme Court of the United States for authority to file its appended brief amicus curiae. (Brief, p. 1).

decision below3/ and has shown in its briefs in opposition to the petitions herein that no compelling reason exists or has been demonstrated for the issuance of a writ of certiorari in this matter.4/

3/ Mid-Louisiana Gas Company, et al. v. Federal Energy Regulatory Commission, 664 F.2d 530 (5th Cir., 1981).

4/ On May 25, 1982, CIG filed its Brief in Opposition to the Petitions for Writ of Certiorari filed by Public Service Commission of the State of New York, No. 81-1889, Arizona Electric Power Cooperative, Inc., No. 81-1958, and The State of Michigan, No. 81-2042.

On August 4, 1982, CIG filed its Brief in Opposition to the Petition for Writ of Certiorari filed by the United States Solicitor General on behalf of the Federal Energy Regulatory Commission, No. 82-19.

NRECA had notice of the originating Commission proceedings.5/ NRECA did not file a petition to intervene in the Commission proceedings below before the United States Court of Appeals for the Fifth Circuit. No justification is shown by NRECA as to why it could not have protected its asserted interest by being a proper party below and before the Court.

5/ The Commission proceedings at Docket No. RM80-6 began with a Notice of Proposed Rulemaking issued November 14, 1979 which was published in the Federal Register (44 Fed. Reg. 66612, Nov. 20, 1979). The Commission proceedings at Docket No. RM80-7 resulted in the promulgation of final regulations which were originally proposed for comment in November of 1978 and issued as interim regulations on December 1, 1978 (43 Fed. Reg. 56448, December 1, 1978). Publication of these documents in the Federal Register is legally deemed to be notice to all interested parties. 44 U.S.C. § 1507 (1976). See also Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380 (1947).

NRECA's motion and brief amicus curiae contain only arguments which have been presented by the petitions for a writ of certiorari already filed or which are, at best, marginally relevant to the issue presented for review.

NRECA has not demonstrated any expertise on the issue presented for review which is not possessed by the parties who have already filed petitions for a writ of certiorari.

Furthermore, NRECA does not demonstrate or reveal in its motion or brief appended thereto any substantial reason why its participation will uniquely aid the court in disposing of these petitions for a writ of certiorari.

In conclusion, the subject motion should be denied for failure to demonstrate an interest or sufficient grounds for the relief sought.

Respectfully submitted,

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Dated: August 19, 1982

Respondent's Reply Brief

5

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IN THE

Supreme Court of the United States

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The Public Service Commission Of The State Of New York, *et al.*,

Petitioners,

v.

Mid Louisiana Gas Company, *et al.*,

Respondents.

On Petitions For A Writ of Certiorari To The United States Court of Appeals For The Fifth Circuit

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OBJECTION OF RESPONDENT CONSOLIDATED GAS SUPPLY CORPORATION TO MOTIONS FOR LEAVE TO FILE BRIEFS AMICUS CURIAE

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TABLE OF CONTENTS

PAGE

I. OBJECTIONS 2

A. Public Utilities Commission Of The State Of California *et al* 2

B. Edmond G. Brown, Jr. 3

C. Public Power Group 3

D. National Rural Electric Cooperative Ass'n 4

E. Associated Gas Distributors 4

II. CONCLUSION 5

TABLE OF AUTHORITIES

PAGE

AUTHORITIES

Sup. Ct. R. 36 ..... 2, 4

MISCELLANEOUS

F.B. Wiener, Briefing and Arguing Federal Appeals (1967) 2

Nos. 81-1889, 81-1958, 81-2042, 82-19

IN THE

Supreme Court of the United States

October Term, 1982

The Public Service Commission Of The State Of New York, *et al.*,

Petitioners,

v.

Mid Louisiana Gas Company, *et al.*,

Respondents.

On Petitions For A Writ of Certiorari To The United States Court of Appeals For The Fifth Circuit

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OBJECTION OF RESPONDENT CONSOLIDATED GAS SUPPLY CORPORATION TO MOTIONS FOR LEAVE TO FILE BRIEFS AMICUS CURIAE

Respondent Consolidated Gas Supply Corporation ("Consolidated") hereby objects to the motions of The Public Utilities Commission of the State of California, *et al.*;[1] Edmond G. Brown, Jr., Governor of California; Associated Gas Distributors; Public Power Group; and National Rural Electric Cooperative for leave to file briefs *amicus curiae* in support of the petitions for certiorari. The motions should be denied as tautological.

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[1]Joining with the Public Utilities Commission of the State of California are Pacific Gas and Electric Co., Southern California Gas Co., and San Diego Gas and Electric Co.

I. OBJECTIONS

Rule 36 requires that where consent has not been granted, motions for leave to file a brief *amicus curiae* state the nature of the applicant's interest, and set forth "facts or questions of law that have not been, or reasons for believing that they will not adequately be, presented by the parties, and their relevancy to the disposition of the case.[2] As shown below, none of the above-listed *amici* have complied with this rule. Instead, their briefs are nothing more than crusaders' efforts to exert extrajudicial pressure on the Court.[3]

Briefs *amicus curiae* are particularly inappropriate in this case. The four Petitioners cut across the entire universe of persons potentially affected by the decision of the court below—the FERC; the State of Michigan; Arizona Electric Power Cooperative; and the Public Service Commission of the State of New York. It is difficult to envision a position that has not already been taken, or an agrument that has not already been made. None of the *amici* has identified one. And, significantly, none of the *amici* chose to participate as parties in the proceedings below. In a case such as this, which arises out of an agency rulemaking interpreting a statute, the place for input is at the agency level, not in the Supreme Court of the United States. *Amici* here seek to transform this Court into a super-agency by presenting fundamental arguments that should have been made below.

A. Public Utilities Commission Of The State Of California et al.

Amici concede that their role is one of "me too":

> We recognize that some of the matters raised in the accompanying amici curiae

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[2] *SUP. CT. R.* 36.

[3] See *F.B. WIENER, BRIEFING AND ARGUING FEDERAL APPEALS* 269 (1967).

> brief may be addressed in the petitions for a writ of certiorari on file or to be filed with this Court.[4]

Yet, *amici* urge the Court to accept the brief because of their unique ability "to inform this Court of the gross inequities which would result from the Court of Appeals decision and to establish that the Court of Appeals views are inconsistent with the mandate of the NGPA."[5] The brief reveals no more insight into the alleged "inequities" and "inconsistencies" than that already provided to the Court by Petitioners.

B. Edmond G. Brown, Jr.

In support of his motion for leave to file a brief *amicus curiae*, Edmond G. Brown, Jr., Governor of California, identifies no fact or question of law that has not already been presented by Petitioners. Governor Brown states as his reason for filing the brief his "ability to provide this Court insight into the legislative deliberations which led to enactment of the NGPA".[6] As is evident from Governor Brown's brief, no more is offered than a summary of various statutory provisions, a recitation of certain sections of the Federal Energy Regulatory Commission's orders, references to the petition filed by Arizona Electric Power Cooperative, Inc., and unsupported hyperbole of a $200 million dollar impact on California consumers.

To suggest that Governor Brown can better present this case to the Court than can the Solicitor General of the United States is presumptuous, at best.

C. Public Power Group

The Public Power Group submitted its brief without the consent of the parties and without having filed a

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[4]Motion of Public Utilities Comm'n of the State of California at 4.

[5]*Id.*

[6]Motion of Governor Brown at 2.

motion for leave to file a brief *amicus curiae*. The rules of this Court require, when consent of the parties has not been granted, that a brief *amicus curiae* may be filed only if accompanied by a motion for leave to file.[7] Respondent Consolidated is a party and did not grant its consent to Public Power Group.

Additionally, a review of the brief discloses nothing by way of fact or law that has not already been offered to the Court in the four petitions for certiorari.

D. National Rural Electric Cooperative Ass'n

NRECA asserts that it has an interest in this case because "many of its member cooperatives are served by federally regulated interstate gas pipelines or state regulated intrastate pipelines and local distribution companies". That status is not unique. Virtually every homeowner or consumer in the United States would qualify as a person served by an interstate pipeline, an intrastate pipeline or a local distribution company. NRECA's conclusory statement that its interests are not adequately represented is not supported by its motion. The "facts" asserted by NRECA (that the impact of the court's decision ranges from $100 million annually to over $12 billion over the life of the reserves) are not only unsupported but are taken directly from the petitions filed by the Federal Energy Regulatory Commission and Arizona Electric Power Cooperative, Inc. This brief was not filed to assist the Court; rather, it was filed to form part of a "cheering section" for Petitioners.

E. Associated Gas Distributors

AGD argues that its motion should be granted because the decision below will have "serious and far reaching implications for the pricing stability of interstate supplies" in that it will result in the abandonment of "the lower, cost-of-service pricing of

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[7] *SUP. CT. R.* 36.3.

significant volumes of pipeline-owned affiliate production".[8]

AGD misunderstands the case. The Commission has not disputed that pipeline affiliate production is entitled to NGPA maximum lawful prices. See Order No. 58, App. B-9. That affiliates of pipelines may charge and collect NGPA prices subject, of course, to the restrictions of NGPA § 601(a)(1)(E) is not disputed. Accordingly, AGD's "unique perspective on this issue" is of no value to the Court.

II. CONCLUSION

Amici have failed to satisfy the minimum standards of this Court's rules for granting leave to file a brief *amicus curiae*. No new facts have been presented to the Court and no legal question not already briefed in the four petitions for certiorari has been raised.

The motions should be denied.

Respectfully submitted,

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[8]AGD Motion at iii.

Respondent's Reply Brief

6

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No. 81-1889

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

THE PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK, *Petitioner*,

v.

MID-LOUISIANA GAS COMPANY, *et al.*, *Respondents*.

**On Petitions for a Writ of Certiorari
To the United States Court of Appeals
For the Fifth Circuit**

BRIEF OF RESPONDENT KANSAS-NEBRASKA NATURAL GAS COMPANY, INC. IN OPPOSITION TO BRIEF OF AMICI CURIAE STATE OF KANSAS AND KANSAS CORPORATION COMMISSION

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TABLE OF CONTENTS

	Page
INTRODUCTION	1
QUESTION PRESENTED	2
ARGUMENT	2
CONCLUSION	4

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1889

THE PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK, *Petitioner*,

v.

MID-LOUISIANA GAS COMPANY, *et al.*, *Respondents*.

**On Petitions for a Writ of Certiorari
To the United States Court of Appeals
For the Fifth Circuit**

BRIEF OF RESPONDENT KANSAS-NEBRASKA NATURAL GAS COMPANY, INC. IN OPPOSITION TO BRIEF OF AMICI CURIAE STATE OF KANSAS AND KANSAS CORPORATION COMMISSION

INTRODUCTION

Respondent Kansas-Nebraska Natural Gas Company, Inc. (Kansas-Nebraska) is filing in this proceeding a joint brief with Michigan Wisconsin Pipe Line Company (Michigan Wisconsin) in opposition to petitions for a writ of certiorari filed by the Public Service Commission of the State of New York *et al.* in Docket Nos. 81-1889 *et al.*[1]

[1] See that brief for the listing of Kansas-Nebraska's affiliates required by Rule 28.1.

However, the State of Kansas and the Kansas Corporation Commission (KCC) have filed a motion for leave to file a brief "amicus curiae" and an accompanying brief which, while it generally supports the petition for writ of certiorari filed by the Public Service Commission of the State of New York, purports to supplement that brief with an argument addressed to the "implications and consequences" which it is perceived that the December 23, 1981 decision of the United States Court of Appeals for the Fifth Circuit "may have on traditional ratemaking." In particular, the State of Kansas and the KCC have illustrated their concerns by reference to an application for a rate increase now pending before the KCC filed by Kansas-Nebraska. (Kansas-Nebraska is a distributor in Kansas, and is regulated as such by the KCC, in addition to being an interstate pipeline regulated by the Federal Energy Regulatory Commission.)

QUESTION PRESENTED

Whether the State of Kansas and the Kansas Corporation Commission have presented any considerations which support the grant of a writ of certiorari in this proceeding.

ARGUMENT

This case involves the interpretation of a definition in the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. (Supp. IV) §§ 3301 *et seq.*—the definition of the term 'first sale' in Section 2(21) of that Act. That question is not even addressed in the brief of the State of Kansas and the KCC.

Instead, the State of Kansas and the KCC advance an argument that "cost of service treatment is the only appropriate method which can or should be utilized for ratemaking purposes." That argument was rejected by

the Congress when it adopted Title I of the NGPA in 1978. (See joint brief of Kansas-Nebraska and Michigan Wisconsin for full discussion.) Even prior to that time, the Federal Power Commission had rejected the cost-of-service approach for most pipeline produced gas and, instead, had been relying on "composite cost based" area and national rates. For reasons described by the Fifth Circuit, Congress abandoned that approach:

> "The fuel shortages of the 1970s revealed two flaws in the regulation of gas production. The first appeared when the area and national rates established by the Commission for gas sold on the interstate market fell markedly below the price available for gas sold on the intrastate market, which was not regulated by the Commission. The price disparity between the two markets skewed the distribution of gas and resulted in shortages of gas available for interstate sale. . . . The second became apparent when the area and national rates established by the Commission did not provide a sufficient incentive to encourage exploration for new sources of gas."[2]

The failure of a method of rate regulation based on historical costs to provide the incentives necessary to encourage exploration for new sources of gas can be illustrated by the ratemaking approaches which the KCC itself has traditionally applied. One example will suffice. A successful exploration program requires the acquisition and maintenance of a "bank" of undeveloped leases, but the KCC refuses to permit Kansas-Nebraska to include undeveloped leases in its rate base.[3]

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[2] Mid-Louisiana Gas Company v. Federal Energy Regulatory Commission, 664 F. 2d 530, 533 (5th Cir. 1981, *rehearing denied*, 1982).

[3] State Corporation Commission of the State of Kansas, Docket No. 113,421-U, Order issued March 12, 1979, page 12.

CONCLUSION

In the Natural Gas Policy Act of 1978 Congress created a new regime for the natural gas industry which is deliberately *not* based on "cost of service" regulation. The fact that the Kansas Corporation Commission might prefer to continue to regulate gas utilities as it has in the past is not relevant to this proceeding and provides no basis for granting its petition for a writ of certiorari.

Respectfully submitted,

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Petitioner's Brief

1

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Nos. 81-1889, *et al.*

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*,

Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,

Respondents.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

BRIEF FOR PETITIONER THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

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QUESTION PRESENTED

Title I of the Natural Gas Policy Act of 1978 prescribes a series of ceiling prices for "first sales" of natural gas. The question presented in this case is whether the Federal Energy Regulatory Commission properly determined that pipeline produced gas which, along with gas purchased from independent producers and other pipelines, becomes part of the pipeline's general system supply for eventual resale to the pipeline's customers, does not qualify for first sale treatment and that, contrary to the court below, it was not required to impute a first sale to the intracorporate transfer of gas between the pipeline's operating divisions.

PARTIES BELOW

American Gas Association
Arizona Electric Power Cooperative and City of Wilcox
Ciba-Geigy Corporation
Colorado Interstate Gas Company
Columbia Gas Transmission Corp.
Consolidated Gas Supply Corp.
Ecee, Inc.
El Paso Natural Gas Company
The Federal Energy Regulatory Commission
Kansas-Nebraska Natural Gas Company
Kansas State Corporation Commission
Kentucky-West Virginia Natural Gas Company
Michigan-Wisconsin Pipe Line Company
Mid-Louisiana Gas Company
Natural Gas Pipeline Co. of America
Northern Natural Gas Company
Northwest Pipeline Corp.
The Public Service Commission of the State of New York
The Public Service Commission of Wisconsin
The State of Michigan and The Public Service Commission of Michigan
Southern Natural Gas Company
United Gas Pipe Line Corp.

TABLE OF CONTENTS

QUESTION PRESENTED i
PARTIES BELOW ii
TABLE OF AUTHORITIES iv
OPINIONS AND ORDERS BELOW 1
JURISDICTION 2
STATUTES AND REGULATIONS INVOLVED 2
STATEMENT OF THE CASE 2
1. The Regulatory Background 2
2. The Natural Gas Policy Act of 1978 5
3. The Proceedings Below 6
SUMMARY OF ARGUMENT 8
ARGUMENT 10
I Preliminary Statement 10
II The Commission's Conclusion That Pipeline Production Qualifies For First Sale Ceiling Rates Only When It Is The Subject Of Discrete Sales Comprised Exclusively Of The Pipeline's Own Production Is Consistent With The Language And Legislative History of The Act 12
III Neither The Act Nor Its Legislative History Support The Imputation Of A Sale To The Intracorporate Transfers Of Pipeline Production Prior To Its Sale To The Pipeline's Customers 29
IV There Is No Valid Basis For Construing Section 2(21) Of The NGPA As Imputing A Separate First Sale To The Portion Of The Subsequent Sale From A Pipeline's System Supply Representing Its Own Production 33
CONCLUSION 36
APPENDIX A-1

TABLE OF AUTHORITIES

JUDICIAL DECISIONS:

Alexander v. FERC, 609 F.2d 543 (D.C. Cir. 1979) 25

Butler v. Thompson, 92 U.S. (2 Otto) 412 (1875) 25

Helvering v. Nebraska Bridge Supply & Lumber Co., 115 F.2d 288 (8th Cir. 1940) 25

Phillips Petroleum Company v. Wisconsin, 347 U.S. 672 (1954) 2, 3, 5

Wells v. 10-X Manufacturing Co., 609 F.2d 248 (6th Cir. 1979) 25

ADMINISTRATIVE DECISIONS:

Canadian River Gas Co, et al., 3 F.P.C. 32 (1942) *aff'd sub nom., Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581 (1945) 2

Columbia Gas Transmission Corporation, Opinion No. 74, 20 F.P.S. 5-495 (February 12, 1980) 35

Just and Reasonable National Rates for Sales of Natural Gas, 52 F.P.C. 1604 (1974), *aff'd, Shell Oil Company v. FPC*, 520 F.2d 1061 (5th Cir. 1976), *cert. denied*, 426 U.S. 941 (1976) 4

Kansas-Nebraska Natural Gas Company, 53 F.P.C. 1694 (1975) 35

Kansas-Nebraska Natural Gas Company, 54 F.P.C. 923 (1975) 4

National Rates for Jurisdictional Sales of Natural Gas, 56 F.P.C. 509 (1976), *aff'd sub nom., American Public Gas Ass'n v. FPC*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978) 3

Permian Basin Area Rate Proceeding, 34 F.P.C. 159 (1965), *aff'd, Permian Basin Area Rate Cases*, 390 U.S. 747 (1968) 3

Pipeline Production Area Proceeding (Phase I), 42 F.P.C. 738 (1969), *aff'd, City of Chicago v. FPC*, 428 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972) 4

STATUTES:

Natural Gas Act
Section 7(c), 15 U.S.C. §717f(c) 2, 26, 35

Natural Gas Policy Act of 1978, 15 U.S.C. §§3301 *et seq.*:

Section 2(20), 15 U.S.C. § 3301(20) ..... passim
Section 2(21), 15 U.S.C. §3301(21) ..... passim
Section 101(b)(9), 15 U.S.C. §3311(b)(9) 6, 13
Section 102, 15 U.S.C. §3312 ..... 14, 20
Section 103, 15 U.S.C. §3313 ..... 14, 20
Section 104, 15 U.S.C. §3314 ..... 14, 21, 22
Section 105, 15 U.S.C. §3315 ..... 14, 20, 21
Section 106, 15 U.S.C. §3316 ..... 14, 20, 21, 22
Section 107, 15 U.S.C. §3317 14
Section 108, 15 U.S.C. §3318 20
Section 121, 15 U.S.C. §3321 ..... 20, 26
Section 203, 15 U.S.C. §3343 ..... 9, 30, 31
Section 315, 15 U.S.C. §3375 26
Section 501, 15 U.S.C. §3411 ..... 10, 32
Section 506, 15 U.S.C. §3416(b) 7
Section 601(b)(1)(E), 15 U.S.C. §3431(b)(1)(E) 20, 21, 26, 27
Section 602(a), 15 U.S.C. §3432(a) 23, 29

Department of Energy Organization Act
Section 403(d), 42 U.S.C. §7173(d) 16

Rules and Regulations of the Federal Energy Regulatory Commission:
18 C.F.R. §154.42 7
18 C.F.R. §270.203(a) 12, 24
18 C.F.R. §301(k) 31
18 C.F.R. §303(c) 31

Federal Energy Regulatory Commission Interim Regulations Under the Natural Gas Policy Act of 1978, 43 Fed. Reg. 56,448, *et seq.* (1978) 6, 7

Pricing of Pipeline Production Under the Natural Gas Act, Docket No. RM80-6, Notice of Proposed Rulemaking, 44 Fed. Reg. 66,612 (1979) 6, 7

LEGISLATIVE HISTORY:

123 Cong. Rec. 29,791 (1977) 23
124 Cong. Rec. S. 16,323 (daily ed. Oct. 4, 1977) . 19, 20
124 Cong. Rec. H. 13,117 (daily ed. Oct. 14, 1978) .. 14
124 Cong. Rec. H. 13,120 (daily ed. Oct. 14, 1978) .. 30

President Carter's Energy Message to Congress 13 Weekly Comp. Pres. Doc. 566 (April 22, 1977) .. 17

H.R. 1758, 81st Cong., 2d Sess., vetoed April 15, 1950, H.R. Doc. No. 555, 81st Cong., 2d Sess. 5

H.R. 6645, 84th Cong., 2d Sess., vetoed February 17, 1956, H.R. Doc. No. 342, 84th Cong., 2d Sess..... 5

H.R. 8444, 95th Cong., 1st Sess. (1977) 17, 18
H.R. 6831, S.2104, 95th Cong., 1st Sess. (1977) . 17, 19

H.R. Rep. No. 539, 95th Cong., 1st Sess. *reprinted in* 1977 U.S. Code Cong. & Ad. News 948 17

H.R. Rep. No. 496, Part 4, 95th Cong., 1st Sess. (1977) 9, 18

S. Rep. No. 1126, 95th Cong., 2d Sess. (1978) .6, 13, 25

H.R. 6381, *et al.* Hearings Before the Subcommittee on Energy and Power of the House Committee on Interstate and Foreign Commerce, 95th Cong., 1st Sess., Part 2 at 967-68 (Statement of Mr. Journey, Commission General Counsel) 19

MISCELLANEOUS:

U.C.C. §2-106 25

U.C.C. §2-304(1) 25

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BRIEF FOR PETITIONER THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

The Public Service Commission of the State of New York (New York), herewith files its brief in this consolidated proceeding.

OPINIONS AND ORDERS BELOW

The opinion of the United States Court of Appeals for the Fifth Circuit from which certiorari was granted (P.A. A-1)[1], is reported at 664 F.2d 530. The Federal Energy Regulatory Commission's Orders Nos. 58, 98 and 102, which were vacated by the opinion below, are not reported but are set out in the Appendix at P.A. B-1, P.A. B-14, and P.A. B-50, respectively.

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[1]References in this brief to the Appendix to the Petition for Certiorari in No. 81-1889 are listed as "(P.A. ___)."

JURISDICTION

The judgment of the court of appeals below was entered on December 23, 1981 (P.A. A-1). On January 11, the court extended the time for petitions for rehearing until January 20, 1982 (P.A. C-2). Petitions for rehearing and suggestions for rehearing *en banc* were denied on February 5, 1982 (P.A. C-3). Timely petitions for certiorari filed by New York, among others, were granted by this Court on October 4, 1982. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) and 15 U.S.C. § 3416(a)(4).

STATUTES AND REGULATIONS INVOLVED

The relevant portions of the Natural Gas Policy Act of 1978, 15 U.S.C. §3301, *et seq.*, and the Regulations of the Federal Energy Regulatory Commission adopted pursuant thereto, are set out in the Appendix to this brief.

STATEMENT OF THE CASE

This case involves an opinion of the Court of Appeals for the Fifth Circuit (P.A. A-1) vacating Order No. 58 of the Federal Energy Regulatory Commission establishing rules governing the pricing of production by interstate pipelines and their affiliates under the Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. §3301, *et seq.* (P.A. B1-B13). An understanding of the issues presented by the opinion below can be facilitated by a brief discussion of the regulatory background prior to the enactment of the NGPA.

1. The Regulatory Background

Regulation of pipeline production operations under the Natural Gas Act, 15 U.S.C. § 717, *et seq.*, followed quite a different course than that of independent producers. Prior to this Court's opinion in *Phillips Petroleum Company* v. *Wisconsin*, 347 U.S. 672 (1954), the Commission believed it had no jurisdiction over the rates for sales of natural gas *to* a pipeline. However, from the inception of regulation under the Natural Gas Act in 1938, the costs incurred *by* pipelines in producing their own gas had been included in the cost-of-service upon which their rates to their customers were based. *Canadian River Gas Co., et*

al., 3 F.P.C. 32 (1942), *aff'd sub nom., Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945). This did not take the form of determining a "just and reasonable" price for each unit of gas produced; rather all of the pipelines' prudent production costs were either capitalized or expensed regardless of the success or failure of their efforts. This methodology essentially removed the risk of failure from the pipelines' production operations since they earned a fair return on all prudent production investments regardless of the success of the ventures.

The regulation of the prices at which independent producers sold gas to the pipelines which emerged after *Phillips, supra,* followed a different regulatory path. Under the "area" and subsequent "nationwide" rate approach, as initially established in the *Permian Basin Area Rate Proceeding*, 34 F.P.C. 159 (1965), *aff'd, Permian Basin Area Rate Cases*, 390 U.S. 747 (1968), and carried over with some modifications in subsequent producer proceedings, a two price system was adopted establishing ceiling rates for each Mcf of flowing or new gas sold, with the flowing gas rates based primarily upon average industry historical costs and the higher new gas rates reflecting the average current cost of developing and producing gas. *Permian Basin Area Rate Cases, id; National Rates for Jurisdictional Sales of Natural Gas*, 56 F.P.C. 509 (1976), *aff'd sub nom., American Public Gas Ass'n.* v. *FPC*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978). Unlike cost-of-service pricing, the area or national rates were unit rates applied to each Mcf of gas sold. This methodology placed the risk of failure upon the producer.

There has always been a portion of pipeline-owned gas production which did not become part of system gas supply but which was sold at or near the wellhead in what is known as "field" or off-system sales. Some pipelines have contracted with the landowners from whom they secured production leases or over whose properties pipes were laid, as part of the royalty of right-of-way agreements, to sell a portion of the pipeline's gas production for the landowner's use. In addition, pipelines not infrequently develop gas which, because of a combination of inadequate volumes and distance from the pipeline's existing facilities,

is uneconomical to attach to the pipeline's system. In such circumstances, they have often been able to contract to sell this gas production off-system to other pipelines, local distributors or end users with closer facilities or otherwise able to make economic use of the gas. Such sales, many of which are direct or intrastate sales not subject to the Commission's rate jurisdiction under the Natural Gas Act, have always been treated as if they were wellhead sales by independent producers of natural gas rather than priced on a cost-of-service basis.

In 1964, the Commission instituted a proceeding to determine whether it was reasonable within the governing standards of the Natural Gas Act to modify its established cost-of-service methodology for pricing pipeline production in the light of the ongoing area rate proceedings involving producer sales to pipelines. In *Pipeline Production Area Proceeding (Phase I)*, 42 F.P.C. 738, 1089 (1969) *aff'd, City of Chicago* v. *FPC*, 458 F.2d 731 (D.C. Cir. 1971) *cert. denied*, 405 U.S. 1074 (1972), the Commission concluded that with respect to pipeline production from leases acquired after the date of its determination (October 8, 1969), the public interest in encouraging pipeline production would be served by pricing such gas at the appropriate rate applicable to sales of gas by independent producers. It also made clear that it would continue to apply the area rate to pipeline production sold "off-system" at the wellhead to other pipelines. 42 F.P.C. at 746. However, this holding was not made applicable to pipeline production from the pre-October 8, 1969 leases. Production from such leases continued to be priced on a cost-of-service basis.[2] In addition, certain pipelines were authorized, pursuant to a showing of special circumstances, to price some of their production from newer wells or leases on a cost-of-service basis. See *Kansas-Nebraska Natural Gas Company*, 54 F.P.C. 923, 925-27 (1975).

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[2]The one exception is that in 1974 the Commission concluded that pipeline production on old leases from wells commenced after January 1, 1973, would secure the nationwide rate. *Just and Reasonable National Rates for Sales of Natural Gas*, 52 F.P.C. 1604, 1656 (1974), *aff'd, Shell Oil Company* v. *FPC*, 520 F.2d 1061 (5th Cir. 1976), *cert. denied*, 426 U.S. 941 (1976).

2. **The Natural Gas Policy Act of 1978**

The issue of the extent to which the prices at which producers of natural gas sell their gas to interstate pipelines should be subject to federal regulation has been a matter of controversy ever since *Phillips, supra.* Twice in the 1950's, Congress passed legislation eliminating such regulation, but in both cases the bills were subject to Presidential veto. In each case, the issue of pipeline production was expressly addressed. The 1950 bill[3] excluded pipeline production from the proposed deregulation. The 1956 bill[4] contained a separate provision (as a new Section 5(f) of the Natural Gas Act) specifying that in rate proceedings the pipeline would be allowed to recover the reasonable market price of any gas produced by it as an operating expense.

Legislation to modify the nature of producer regulation became a live issue again in the mid-1970's in the light of curtailment of pipeline service stemming from inadequate interstate gas supplies coupled with the general energy crisis resulting from the rapid increase in oil prices caused by the formation of OPEC. Various and conflicting proposals were advanced ranging from complete deregulation to imposition of federal control over sales in the intrastate market exempted from regulation under the Natural Gas Act. However, throughout the more than two-year period in which the compromise legislation which became the NGPA was before the Congress, no sponsor of legislation and no pipeline expressed any dissatisfaction with the existing regulation of pipeline production or suggested that the cost-of-service treatment of some of this production was operating in a manner contrary to the public interest and should be eliminated.

The legislation that emerged as the NGPA provided in Title I for a series of "maximum lawful ceiling rates" for various categories of "first sales" of natural gas, with some categories to be deregulated at specified dates and others to remain subject to

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[3]H.R. 1758, 81st Cong., 2d Sess., vetoed April 15, 1950, H.R. Doc. No. 555, 81st Cong., 2d Sess.

[4]H.R. 6645, 84th Cong., 2d Sess., vetoed February 17, 1956, H.R. Doc. No. 342, 84th Cong., 2d Sess.

regulation. Pursuant to the provisions of Section 101(b)(9), 15 U.S.C. §3311(b)(9), these rates were to be available only to the extent they did not exceed the contract price for the first sale. The term "first sale" was defined in Section 2(21), 15 U.S.C. §3301(21) as the sale of any volume of gas *to* an interstate or intrastate pipeline, local distribution company or end user, but as not including any sale *by* an interstate or intrastate pipeline, local distribution company or affiliate thereof "unless such sale is attributable to volumes of natural gas produced" by such an entity. Neither the Conference Report on the bill[5] nor any other statement in the legislative history provides any further elucidation of this language.

3. **The Proceedings Below**

The NGPA was enacted into law on November 9, 1978, with the pricing provisions of Title I to be effective on December 1, 1978. On November 28, 1978, the FERC issued Interim Regulations governing the implementation of Title I of the Act.[6] Section 270.203(a) of these regulations, 43 Fed. Reg. 56,549-50, provided that a sale of gas by a pipeline was "attributable" to the pipeline's own production within the meaning of Section 2(21)(B) of the Act only when the sale was comprised of production volumes from identifiable wells, properties or reservoirs owned by the pipeline.

On November 14, 1979, the Commission issued its Order No. 58 in Docket No. RM80-7, which prescribed its "Final Rule Governing the Maximum Lawful Price for Pipeline, Distributor or Affiliate Production" under the NGPA (P.A. B-1). With respect to pipeline production the Commission, rejecting the

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[5]S. Rep. No. 1126, 95th Cong., 2nd Sess., (1978).

[6]43 *Fed. Reg.* 56,448, *et seq.* (1978). on November 15, 1978, the Commission had issued a Notice of Proposed Rulemaking in Docket No. RM79-3 proposing a series of Interim Regulations implementing the NGPA, including a proposal governing the circumstances under which pipeline production would be classified as a first sale somewhat similar to that adopted on November 28, 43 *Fed. Reg.* 53,270-53,410. The date for comments was set as November 20, 1978, but in recognition of the extremely short time for comment, the Commission stated it would receive additional comments within 60 days of issuance of its Interim Regulations which would be considered in reaching its final rules on various aspects of the NGPA.

contrary contentions by a number of pipelines, essentially reaffirmed its determination in the Interim Regulations.[7] Since the Commission recognized that this action would leave most pipeline production subject to its regulatory authority under the Natural Gas Act, it simultaneously issued a Notice of Proposed Rulemaking in Docket No. RM80-6 to consider the extent to which in the exercise of this authority it should price pipeline production at the NGPA levels or adhere to existing procedures and standards for pricing such gas.[8]

On August 4, 1980, the Commission issued Order No. 98, in Docket No. RM80-6, its "Final Rule Governing Pricing of Pipeline Production Under the Natural Gas Act" (P.A. B-14). This Order amended the Commission's Regulations under the Natural Gas Act and added a new Section 154.42, 18 C.F.R. §154.42. The new rule had the effect of pricing all pipeline company-owned and affiliate production (not already qualifying for NGPA first sale treatment under Order No. 58) at the applicable NGPA ceiling rates for independent producer sales of similar gas unless such gas was currently being priced on a cost-of-service basis. This latter category of gas, for which gas consumers had already paid most of the pipeline's cost, was maintained on a cost-of-service basis.

Petitions for rehearing of Order Nos. 58 and 98 were filed by a number of parties, and on October 3, 1980, the Commission issued Order No. 102 which, except for a minor clarification of Order 98 not here material, denied rehearing of both Order No. 58 and Order No. 98 (P.A. B-50).

Separate appeals were then taken by a number of pipelines pursuant to Section 506(b) of the NGPA, 15 U.S.C. §3416(b),

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[7]Contrary to the provisions of Section 270.203(a) of the Interim Regulations, Order No. 58 concluded that all sales by pipeline affiliates, including those to the pipeline, were attributable to the affiliates' production and eligible for Title I ceiling rates if the sales contract authorized their collection.

[8]*Pricing of Pipeline Production Under the Natural Gas Act*, Docket No. RM80-6, *Notice of Proposed Rulemaking*, 44 *Fed. Reg.* 66,612 (1979).

both from Order No. 58 as reaffirmed by Order No. 102 (consolidated in the 5th Circuit under the title *Mid-Louisiana Gas Company, et al.* v. *FERC*, No. 80-3804) and from Order No. 98 as reaffirmed by Order No. 102 (consolidated below under the title *Consolidated Gas Supply Corporation, et al.* v. *FERC*, No. 80-4010). The two sets of cases were argued together and on December 23, 1981, the Court issued its opinion holding that all pipeline production constituted a first sale within the meaning of Section 2(21) and vacating both Order Nos. 58 and 98 (P.A. A-1). By order of February 5, 1982, applications for rehearing or rehearing *en banc* were denied (P.A. C-3).[9]

Petitions for a writ of certiorari filed by New York, the State of Michigan, Arizona Electric Power Cooperative and the Commission were granted by this Court on October 4, 1982.

SUMMARY OF ARGUMENT

The issue in this case is whether the Commission properly concluded that the Congress, in fixing a series of maximum ceiling prices for first sales of natural gas in the NGPA, had not reversed, *sub silentio*, forty years regulation of pipeline production operations under the Natural Gas Act, and that the only sales of the pipeline's own gas production which qualify as first sales as that term is defined in Section 2(21) of the NGPA were off-system sales of discrete volumes of a pipeline's gas production which did not become a portion of system gas supply and which had always been treated like sales by independent producers. The Commission's interpretation of the first sales definition is consistent with the language and legislative history of the Act which sought to prescribe rates for the "first transfer of natural gas for value in an arms-length transaction" in contrast

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[9]The court of appeals vacates Commission Order No. 98 without reaching the issues raised in Case No. 80-4010 (other than an issue as to special relief it found not ripe for review) "because we hold that the Commission lacked authority to set prices for interstate pipeline production under the NGA" (P.A.A.-15). In the event this Court were to find that the court of appeals erred in setting aside Order No. 58, it would be required as well to set aside its vacation of Order No. 98 and to remand the case to the court of appeals for consideration of the challenges to Order No. 98 on their merits.

to "subsequent sales of natural gas that are subject to the jurisdiction of the Federal Power Commission under the Natural Gas Act." (H.R. Rep. No. 496, Part I, 95th Cong., 1st Sess., 103, 108-09.) There is nothing in the legislative hearings, reports or debates which expresses any Congressional or industry dissatisfaction with the existing pricing of pipeline production, or suggests that the Commission's pricing of the oldest and lowest cost pipeline production on a cost-of-service basis under which the pipelines recover all of their prudent investments regardless of the success of their efforts, inhibited optimum production efforts by the pipelines.

There is no basis for the court of appeals' conclusion, rejected by the Commission, that Congress intended the Commission to define as "first sale" the intracorporate transaction within the pipeline where gas is transferred from its production department to the personnel responsible for the pipeline's transmission, storage and sales functions. No sale within the meaning of Section 2(20) of the NGPA or the Uniform Commercial Code is involved in such transfer since there is no contract or agreement between separate entities, no transfer of title and no passage of consideration from buyer to seller. Contrary to the court's opinion, the imputation of a sale to the intracorporate transfer of gas is not required to effectuate either the production enhancing objective of the Act or to eliminate the dual market existing under the Natural Gas Act which had led to the widespread diversion of gas from the interstate market. Nor is the imputation of a first sale to the intracorporate transfer of gas required to give meaning to the final clause of Section 2(21)(B); the regulatory dichotomy between wellhead or field sales of a pipeline's own gas production which does not become a part of its system supply and pipeline sales of system supply of which its own production makes up an indistinguishable part was well established prior to the NGPA and its continuation is consistent with both the language and legislative history of the Act. Finally, contrary to the court of appeals' view, the provisions of Section 203(b)(2) of the NGPA requiring the Commission to prescribe rules determining the first sale acquisition cost of pipeline

production for purposes of the incremental pricing provisions of the Act and the Conference Report language suggesting that the Commission could exercise its general authority to define terms such as "transfer for value" and "establish rules governing intracorporate transactions," support the validity of the Commission's actions in Order No. 58 limiting first sale treatment of pipeline production to actual sales attributable to such production.

The alternative argument by the pipelines below that the Commission is required to impute a separate "first sale" of the pipeline production portion of the gas sold from the pipeline's general system supply to its customers, after transportation and storage from the production areas, is equally without merit. Nothing in the Act or its legislative history supports the contention that the Commission was required to impute a fictitious bifurcation of the subsequent pipeline sales subject to its jurisdiction under the Natural Gas Act in order to provide windfall profits to the pipelines for their oldest and lowest cost gas.

ARGUMENT

I.
Preliminary Statement

The issue in this case is whether the ceiling rates prescribed by Title I of the NGPA for various categories of "first sales" of natural gas are applicable to the gas production of interstate pipelines which, after being commingled with supplies of gas purchased by the pipeline from independent and affiliated producers, is sold by the pipeline to local distribution companies or end users of gas. In Order No. 58 (P.A. B-1), the Commission, which is charged with responsibility for administration and enforcement of the Act by Section 501 of the NGPA, 15 U.S.C. §3411,[10] held that pipeline production did not constitute a

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[10]This authority includes the authority to adopt rules and orders "necessary or appropriate to carry out its functions under the Act and to definte 'accounting, technical and trade terms' in the Act consistent with the Act's own definitions."

"first sale," as that term is defined in Section 2(21) of the Act, except when it is sold under a discrete contract covering gas which is solely attributable to the pipeline's own production, and that the physical transfer of gas within the pipeline itself did not constitute such a sale. Under this definition, the bulk of the pipeline's gas production, which becomes a fungible part of the pipeline's system gas supply acquired from various sources prior to sale to the pipeline's customers, would not qualify for first sale treatment and the pricing of such production would remain subject to the Commission's jurisdiction under the Natural Gas Act. The result of the Commission's rule was to maintain the *status quo* with respect to the pricing of pipeline gas production.[11]

The opinion below reached a different result. The court of appeals concluded that it was not obligated to provide the normal deference to an agency's contemporaneous interpretation of an Act it is empowered to administer because the Commission had not participated in the drafting of the NGPA definition of "first sale," and, in the court's opinion, had no expertise in the area. Reviewing the matter, *de novo*, the court determined that the Act and its legislative history evinced a clear Congressional intent that the transfer of pipeline produced gas from the production "division" to the transportation "division" of a pipeline be characterized as a "first sale" of natural gas eligible to secure the ceiling rates prescribed in Title I of the Act. The result of the court's order imputing a sale to the intracorporate transfer of gas

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[11]As indicated, *supra*, the Commission initiated a supplemental proceeding in Docket No. RM80-7 to determine how it should exercise its continuing authority under the Natural Gas Act over pipeline production not qualifying as a first sale. It concluded in Order No. 98 (P.A. B-14) that pipeline production which it had previously found should be priced at the levels applicable to analogous production of independent producers should now secure NGPA ceiling prices, but that pipeline production previously priced on a cost-of-service basis should continue to receive such treatment. The court below did not find it necessary to pass upon the challenges to this determination since Order No. 98 was necessarily predicated upon the validity of Order No. 58 the court had found to be unlawful.

is to allow pipelines the NGPA ceiling prices for *all* of their production, including their oldest, lowest cost production which had always been priced on a cost-of-service basis. The consequence is an increase in pipeline rates of several hundreds of million dollars a year.

There is no question as to Congress' authority to limit the Commission's jurisdiction under the Natural Gas Act to regulate the pricing of pipeline production. The question is whether Congress did so when it altered the regulatory scheme for determining the price at which independent and affiliated producers could sell natural gas to the pipelines. In the context of forty years of separate modes of pricing sales of natural gas by producers *to* pipelines and the pipelines' own gas production (see *supra* at 2-4) it cannot be presumed that legislation changing the former also repealed the Commission's juriscition under the Natural Gas Act over a pipeline's production operations. Unless the language of the Act required a different result, or the language was ambiguous but the result was compelled by persuasive legislative history, there was no warrant for the court's substitution of its view of what constituted a first sale for that of the Commission. As we show below, both the language and history of the Act in fact support the Commission's interpretation.

II.

The Commission's Conclusion That Pipeline Production Qualifies For First Sale Ceiling Rates Only When It Is The Subject Of Discrete Sales Comprised Exclusively Of The Pipeline's Own Production Is Consistent With The Language And Legislative History of the NGPA

The Commission's "Attribution Rule" adopted in Order No. 58 as Section 270.203(a) of its Regulations, 18 C.F.R. §270.203(a), holds that a sale of pipeline production is a "first sale" within the meaning of Section 2(21) of the NGPA only if the sale is comprised of gas exclusively stemming from identifiable wells, properties or reservoirs owned by the pipeline. This rule, which has the effect of maintaining Commission jurisdiction under the Natural Gas Act over pipeline production which is commingled with system supply before being sold to the

pipeline's customers, is a valid contemporaneous construction of the NGPA by the agency authorized to administer the act and define its terms and is fully consistent with the language, structure and legislative hisotry of the NGPA.

A. **The Statutory Scheme**

A major thrust of Title I of the NGPA was to bring all sales of natural gas within the ambit of federal regulation, thus eliminating the dual market for natural gas which had existed under the Natural Gas Act where, since direct and intrastate sales were not regulated, significant supplies had been siphoned off from the interstate market. At the same time, in order to provide an incentive for increased production of natural gas within the United States without creating unnecessary windfalls for the producers, Title I provided for a series of maximum ceiling rates for first sales of new and high-cost natural gas substantially in excess of current levels, and eventual deregulation of most categories of such gas, while maintaining the prices for most old flowing gas at current levels, plus a specified inflation factor.

Not all sales of natural gas are covered by Title I of the Act but only "first sales." Moreover, the maximum lawful prices for the various categories of "wellhead sales" set forth in Title I[12] are, as the Act specifies, only "ceiling rates," with the actual rate which a producer can charge for any first sale being determined by its sales contract. This is made clear by the provisions of Section 101(b)(9) of the Act, 15 U.S.C. §3311(b)(9), which provides that the maximum lawful prices established under Title I "shall not supersede or nullify the effectiveness of the price" which is "established under any contract for the first sale of natural gas" as long as the price thereunder does not exceed the ceiling price. The importance of this provision in limiting the charges for first sales to those necessary as an incentive to optimum production and avoiding unnecessary windfalls was stressed in the Conference Report on the NGPA, S. Rep. No. 1126, 95th Cong. 2d Sess.

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[12]Title I of the NGPA (subchapter I in the nonmenclature of the U.S. Code) is entitled "Wellhead Pricing" and Subtitle A (Part A of the Code) "Wellhead Price Controls."

(1978) (hereinafter "Conference Report") which states at page 74:[13]

> The rule for application of ceiling prices pertains to maximum lawful prices. All maximum lawful prices are ceiling prices only. In no case may a seller receive a higher price than his contract permits.

While Title I prescribes maximum ceiling rates for all first sales of natural gas, there is a marked difference between the ceilings applicable to "new" gas and various types of "high-cost" gas and those applicable to older flowing gas. New gas subject to Sections 102 and 103 of the Act, 15 U.S.C. §§3312 and 3313, and most high-cost gas priced under Section 107, 15 U.S.C. §3317, is subject to eventual deregulation under Section 121, 15 U.S.C. §3321, and the ceiling prices for such gas for the periods in which it remains subject to regulation are established at levels substantially in excess of those prevailing under the nationwide rates prescribed by the Commission at the time the NGPA was adopted. The ceiling rates for first sales of old flowing gas, both interstate and intrastate, were fixed by Sections 104, 105 and 106 of the Act, 15 U.S.C. §§3314-3316, at the effective rate as of April 1977 (or in the case of intrastate sales at the date of enactment) plus a specified inflation factor. The one exception was with respect to so-called "stripper-well" gas from wells producing less than 60 Mcf of gas per day where, to encourage continued production of economically marginal properties, the ceiling rate was fixed at a substantially higher level.

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[13]See also the "Explanation Statement" of Congressman Dingell, one of the House managers of the bill submitted by the Joint Conference Committee, 124 Cong. Rec. H. 13117 (daily ed. Oct. 14, 1978):

> "...The rule set forth in Section 101(b) (9) is that the legislation establishes *ceiling* rates. Contract prices may be lower than the federal lawful maximum price. In such cases, the contractual arrangement between the parties continues to govern their relationship and is not superseded by the federal ceiling prices. Thus, contract prices are superseded only in those instances in which the ceiling price is less than the contract price."

Since both the Commission and the court of appeals agree that pipeline production qualifies for the ceiling prices prescribed in Title I only to the extent it can properly be characterized as involving a "first sale," we turn to the definitions of the terms "sale" and "first sale" in the Act. "Sale" is defined in Section 2(20), 15 U.S.C. §3301(2)(20), simply as "any sale, exchange or transfer for value." The more complex definition of "first sale" in Section 2(21), 15 U.S.C. §3301(2)(21) is as follows:

> (A) **General rule.**—The term "first sale" means any sale of any volume of natural gas—
>
> (i) to any interstate pipeline or intrastate pipeline:
> (ii) to any local distribution company;
> (iii) to any person for use by such person;
> (iv) which precedes any sale described in clauses (i), (ii), or (iii); and
> (v) which precedes or follows any sale described in clauses (i), (ii), (iii) or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this chapter.
>
> (B) **Certain sales not included.**—Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

Both of these definitions of the terms "sale" and "first sale" originated in the Joint Conference on the bill which resulted in the NGPA. Neither term is further explained in the Conference Report.

Subsection A of the first sale definition is all inclusive. Clauses (i)-(iii) cover sales *to* interstate and intrastate pipelines, local distribution companies and end users, thus eliminating the situation under the Natural Gas Act where some of such sales were exempt from the federal regulatory scheme. Clause (iv) is

apparently intended to cover the situation where a series of sales are made by producers prior to the sale to a pipeline, distributor or end user[14] and makes clear all such sales are subject to the ceiling price limitations. Clause (v) gives the Commission the authority to classify as a first sale any prior or subsequent sale which would otherwise not be a first sale in order to prevent circumvention of the maximum lawful rates prescribed by Title I.

The very all inclusiveness of Subsection A necessitated the exclusionary language of Subsection B since, if all sales *by* interstate or intrastate pipelines or local distributors to other pipelines, distributors or end users were first sales, the rates which pipelines and distributors could charge for these sales to their customers would be limited to the ceiling prices and could not include their operating costs plus a return on their investment. Subsection B resolves this problem by excluding from the first sale classification all sales by interstate and intrastate pipelines, local distribution companies or their affiliates, "unless such sale is attributable to volumes of natural gas produced," by one of such entities. The coverage of the "unless clause", which is not further elucidated in the Conference Report, is the specific area of controversy in this case. Before turning to the Commission's construction in Order No. 58, and the opposing views of the court of appeals and pipeline respondents, it is useful to review the legislative history of the term "first sale" since it casts considerable light upon the Congress' underlying intent.

B. The Legislative History

To the best of our knowledge, the first use of the term "first sale" in any statute involving natural gas was in 1977 in Section 403(d) of the Department of Energy Organization Act, 42 U.S.C. §7173(d). This section provides that the Commission may afford interested parties an opportunity to submit written questions on

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[14]Thus, producers frequently sell their gas to larger producers owning processing plants under contracts entitling them to a percentage of the unit price the larger producer receives for sales to pipelines at the "tail gate" of the plant. Under clause (iv), the prices for both sales would have to be within the ceilings.

disputed issues of fact in rulemaking proceedings "to establish rates and charges for the *first sale* of natural gas by a producer or gatherer *to* a natural gas pipeline under the Natural Gas Act" (emphasis added). The words "first sale" are not defined or discussed in the legislative history of the Act. However, the section, which the Conference Report on the bill (H.R. Rep. No. 539, 95th Cong., 1st. Sess. 77, *reprinted in* 1977 U.S. Code Cong. & Ad. News 948)[15] states is applicable to rulemaking proceedings "to set the wellhead price of natural gas," clearly does not relate to sales by pipelines.

The term "first sale" was carried over, again without definition, into the several bills (*e.g.* H.R. 6831, S.2104, 95 h Cong. 1st Sess.) introduced in May 1977 in response to President Carter's Energy Message to the Congress of April 20, 1977, 13 Weekly Comp. Pres. Doc. 566 (1977). Part D of these bills directed the President to establish maximum lawful prices for "any first sale by a producer," with the criteria for such prices varying dependent upon whether the sale was of "new natural gas," "old natural gas under existing contracts" or "old natural gas under new contracts," and authorized the President to establish "special" higher incentive prices for specified categories of high-cost gas or to adjust the maximum lawful prices for first sales where the "producer bears all or part of the cost of transportation or liquefication of such gas." (See H.R. 6831, Sections 404-406, 408). In addition to his authority respecting first sales by a producer of natural gas, the President was authorized to prescribe maximum lawful prices applicable "to any sales of natural gas by any other person" to the extent necessary to prevent circumvention of the ceiling prices established for the first sales by producers. But this authority was expressly made inapplicable "to sales for resale by such other persons if such sales are subject to the Natural Gas Act." (See H.R. 6831, Section 408 (d)).

The legislation (H.R. 8444, 95th Cong., 1st Sess.) which passed the House on August 5, 1977, was similar in structure to the

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[15]The Conference Report refers to the provision as Section 403(c). It was subsequently changed to be Section 403(d).

Administration bill insofar as the first sale pricing provisions were concerned, though a new pricing category relating to first sales of old natural gas under "rollover contracts" was added and the prices for the various categories of first sales, other than high-cost gas where the Commission was authorized to fix the ceiling price, were specified in the statute. In addition, the power to establish rules to prevent circumvention of the first sale pricing limits by subsequent sales not already subject to Commission jurisdiction under the Natural Gas Act was given to the Commission in Section 413(e)(4) of the bill as part of its general rulemaking authority. The intent of the draftsmen of the bill was made clear in the report of the Committee on Interstate and Foreign Commerce (H.R. Rep. 496, Part 4, 95th Cong., 1st Sess. (1977) at 103, 108-109) as follows:

> *Maximum Law Price - First Sale Concepts*
>
> Part D establishes "maximum lawful prices" applicable to certain categories of "first sales" of natural gas sales contracts. *The Committee intends that the term "first sale" be applied by the Federal Power Commission to the first transfer of natural gas for value in an arms length transaction.* Therefore, the first sale price is essentially a wellhead price.
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> * * * * * * *
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> *Sec. 413 - Administrative Procedure, Enforcement and Judicial Review*
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> * * * * * * *
>
> Section 413 also authorizes the Federal Power Commission to prescribe maximum lawful prices applicable to any sale of natural gas other than sales to which Section 404, 405, 406, 407 or 409 applies, or which are subject to the provisions of the Natural Gas Act, if the Commission determines that a maximum lawful price is necessary to prevent circumvention of any provision of Part D by any person making any sale of natural gas, including, but not necessarily limited to, interstate and intrastate pipeline companies, states, royalty interest owners, and local

> distribution companies. Because Section 404, 405, 406, 407 and 409 apply only to first sales of natural gas, *prices for subsequent sales of natural gas that are subject to the jurisdiction of the Federal Power Commission under the Natural Gas Act will remain regulated by the Federal Power Commission* (emphasis added).[16]

The substitute for the Administration proposal which was adopted by the Senate on October 4, 1977, as a rider to H.R. 5289, 124 Cong. Rec. S. 16,323 (daily ed. Oct. 4, 1977) did not attempt to establish a series of maximum lawful prices for "first sales" of natural gas and does not utilize the term "first sale." It focuses, instead, upon the deregulation of "new natural gas sold or delivered in interstate commerce" and the establishment of interim ceiling rates for the sales in interstate commerce of new natural gas produced from offshore Federal lands where deregulation was to be postponed until January 1, 1982.[17] "Old" gas sold in interstate commerce for resale remained subject to full regulation by the Commission under the Natural Gas Act.[18]

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[16]In the hearings on the Administration bill before the House Committee on Interstate and Foreign Commerce, there was a discussion as to the meaning of the then undefined term "first sale" in which Mr. Journey, the Commission's General Counsel, stated:

> "You won't find it [the term first sale] in the case law, and you won't find it, as far as I know, in the Natural Gas Act. You will find it as a phrase cropping up in the jargon of people who are dealing with wellhead sales, and who are dealing with questions of regulation and deregulation...I read this as meaning wellhead sales."
>
> H.R. 6381, *et al.* Hearings Before the Subcommittee on Energy and Power of the House Committee on Interstate and Foreign Commerce, 95th Cong., 1st Sess., Part 2 at 967-68.

[17]See Amendment 1039, 124 Cong. Rec. 16323 (daily ed. Oct. 4, 1977). All other "new gas" sales in interstate commerce were to be deregulated as of the date of enactment.

[18]*Id.* The one exception was a proposed amendment to Section 5(a) of the Natural Gas Act which would have precluded any Commission order decreasing the rate for the "sale or transfer" of either old or new gas produced from offshore Federal lands where the rate had previously been found to be just and reasonable by the Commission. See H.R. 5289, Section 6.

Provisions requiring the Commission to permit interstate pipelines to passthrough to their customers the costs of new gas purchases were limited in the case of purchases from an affiliate or where the pipeline *"produces new natural gas from its own properties."* to the current rates and charges made, demanded or received for comparable sales by persons not affiliated with the pipeline.[19]

The bill which emerged from the Conference Committee and was subsequently enacted into law as the NGPA essentially adopts the "first sale" pricing structure of the House bill, though two different maximum ceiling prices for first sales of specified types of new natural gas were established in Sections 102 and 103, 15 U.S.C. §§3312 and 3313, special provisions for first sales under existing intrastate contracts were established in Sections 105 and 106(b), 15 U.S.C. §§3315 and 3316(b), and a new provision, providing a higher maximum lawful price for "stripper wells" producing less than 60 Mcf of gas per day became Section 108, 15 U.S.C. §3318. Under Section 121 of the Act, 15 U.S.C. §3321, first sales of gas under Sections 102, 103 and 105 and certain categories of first sales of high-cost gas under Section 107, 15 U.S.C. §3317, were to be deregulated on specified dates. And for the first time, the terms "sale" and "first sale" were defined in Sections 2(20) and 2(21) respectively.

The separate provision of Section 413 of the House Bill which had authorized the Commission to adopt rules to prevent circumvention of the first sale ceiling prices was replaced by Section 2(21) (A) (v) which provided that any sale of any volume of natural gas which precedes or follows any sale otherwise defined as a first sale could itself be defined as a first sale "to prevent circumvention of any maximum lawful price established under this chapter." Finally, while Section 601(b) (1) (E), 15 U.S.C. §3431(b) (1) (E), limited the charges interstate pipelines could passthrough to their customers for gas purchased in first sales from their production affiliates to the amounts paid in comparable first sales between persons unaffiliated with the

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[19] *Id.*

pipeline, no such restriction was placed upon natural gas produced from the pipeline's own properties, as had been the case in the analogous provision of the Senate bill.

C. The Status of Pipeline Production Under the NGPA

With one exception discussed *infra* at 30-31, the only mention of pipeline production in the NGPA is in the "unless" clause of Section 2(21) (B), which constitutes the exception to the exception from the comprehensive coverage of all sales of natural gas within the meaning of Section 2(21) (A). It is clear that the unless clause was intended to cover some types of gas production by interstate and intrastate pipelines, local distribution companies and their affiliates; otherwise, the subsection could have ended with a period before the word "unless." Since the language of the unless clause speaks in terms of "sales attributable to volumes of natural gas produced" by a pipeline, distributor or affiliate thereof, the two constructions of the clause best conforming to normal grammatical concepts would be either to read the language, as the Commission did, as applying to actual sales by any of the named entities where all of the gas is attributable to their own production, or, alternatively, as applying to sales where any portion of the gas is attributable to production by a pipeline, distributor or affiliate. The trouble with this latter alternative is that, while it is a grammatical construction of the unless clause, it results in the complete negation of the first clause of Section 2(21) (B) and obviously suberts the Congressional intent.

The Commission interpretation of the unless clause distinguishes between two types of pipeline, distributor and affiliate production of gas: (1) "first sales" where the gas is sold off-system by contract or exchange agreement to another pipeline, distributor or end user, and (2) where the company-owned production becomes a fungible portion of the seller's overall gas supply. The distinction is wholly consistent with the legislative history of the NGPA set forth above, as well as with the language of the clause. While it results, at least insofar as the production operations of the interstate pipelines are concerned,

in leaving the pricing of most pipeline production subject to the Commission's jurisdiction under the Natural Gas Act,[20] this reflects the pre-existing distinction between the types of pipeline sales and the regulatory treatment thereof which the NGPA carefully maintained.

On a more pragmatic level, the Commission's interpretation of the "unless" clause furthers the Congressional objectives of providing the necessary incentives for optimum production efforts and withholding incentives where none are necessary, while the court of appeals' interpretation that all pipeline produced gas is eligible for first sale ceiling rates results in huge windfall profits on old cost-of-service production. As indicated above, the NGPA in Sections 104, 105 and 106 provides for maximum lawful ceiling prices for old flowing gas based on the prices in effect as of April 1977 (or November 1978 in the case of intrastate sales), plus an inflation factor. Higher ceiling prices for such gas were, however, made available under Section 107 where it fell within certain categories of high-cost gas and under Section 108 for low production stripper well gas, on the theory that since the producers making the first sales were not guaranteed a return on their production investment, they would require the additional incentive of the higher rates to cover the cost of such high-cost operations or to make economic the continued operation of marginal stripper wells which would otherwise be abandoned.

With respect to pipeline production priced on a cost-of-service basis, however, such higher incentive prices were unnecessary

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[20]In the case of affiliated production companies, the opposite result stems from the Commission interpretation since such companies normally make initial sales of their gas either to their affiliates or to other pipelines, distributors or end users prior to commingling the gas with gas acquired from other sources. Section 601(b)(1)(E) assures that the lack of arms-length bargaining where their "first sales" are to affiliates does not result in prices in excess of comparable sales between unaffiliated entities.

since the pipelines were already assured of a return of and on their production investment, plus reimbursement of all operating costs regardless of success, and would therefore be assured recovery of all additional expenditures to increase or maintain production. Affording such pipeline production first sale ceiling rates will not serve the objectives of the higher Sections 107 and 108 ceiling prices but would only provide the pipelines with millions of dollars of additional revenues for the existing flowing gas.[21] At the same time, under the Commission interpretation of the unless clause, to the extent it concluded in Order No. 98 that as a matter of policy pipeline production other than that sold off-system at or near the wellhead should be priced on a successful effort basis like the gas purchased under contract from separate producers, the pipeline is entitled in return for assuming the risk that they may not recover their full production costs, to be treated on a parity with similar gas of independent and affiliated producers.

Finally, as the Commission noted (P.A. B-4, B-62, B-64), its construction of the "unless clause" results in the minimum degree of disruption of existing state jurisdiction over the rates charged by intrastate pipelines and local distribution companies for sales which include their own production. While the states' authority to price such production at less than the first sale ceiling levels is maintained by Section 602(a) of the NGPA, 15 U.S.C.

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[21]In the case of pipeline production from leases acquired prior to October 8, 1969, from wells drilled prior to January 1, 1973, which accounts for the great bulk of cost-of-service production under both the pre-NGPA and post-NGPA Commission rules and policies, the main price escalation under the court of appeals decision would result from the eligibility of a large part of this gas for the higher stripper well prices authorized by Section 108 of the NGPA for wells producing less than 60 Mcf of gas per day. The rationale for these higher prices was that the nationwide rates incorproated into the ceilings for older flowing gas established by Sections 104 and 106 of the Act might make continued production of marginal wells uneconomic and would discourage further investment in such wells to enhance additional production. See, *e.g.*, 123 Cong. Rec. 29,791 (1977).

§3432(a),[22] cost-of-service pricing of such gas at rates exceeding the ceiling prices would be precluded under the court of appeals' rationale and any construction of the "unless clause" of Section 2(21)(B) to include sales involving any amounts of gas produced by intrastate pipelines or distributors would jeopardize state regulation over the basic rates that they could charge to their customers.

III.

Neither The Act Nor Its Legislative History Support The Imputation of A Sale To The Intracorporate Transfers Of Pipeline Production Prior To Its Sale To The Pipeline's Customers

The court of appeals, while concluding that Commission Order No. 58 effectively reads the "unless clause" of Section 2(21) out of the Act (P.A. A-8), did not adopt the arguments by the pipeline petitioners below that the "Attribution Rule" adopted by the Commission, Section 270.203(a), 18 C.F.R. §270.203(a), erred in limiting "first sales" of pipeline production to sales "comprised exclusively of production volumes of natural gas from identifiable wells, properties or reservoirs which are owned by" the pipeline. Instead, the court found unwarranted the Commission's refusal to impute a sale to the intracorporate transfer of gas within the pipeline prior to commingling with gas purchased by the pipeline for sale to the pipeline's customers. In the court's opinion, the "language, purpose and history of the NGPA" demonstrated that Congress intended that all gas production by interstate or intrastate pipelines, local distribution companies or their affiliates "be accorded first sales status" and that this was to be accomplished by treating as a first sale the "intracorporate transfer of pipeline production to the pipeline" (P.A. A-15). As demonstrated below, none of the court's bases for this conclusion are supportable.

In evaluating the opposing views of the Commission and the court below as to whether the intracorporate transfer of gas

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[22]See *Pennzoil Corporation* v. *Public Service Commission of West Virginia*, No. 81-1672, pending on petition for certiorari.

should be characterized as a "sale," the "starting point," as the court otherwise recognized (P.A. A-7), is the definition of sale in Section 2(20) of the NGPA, 15 U.S.C. §3301 (2)(20). This section, which the court neither cites nor discusses, states that the term "sale" as used in the Act means a "sale, exchange or transfer for value." None of these terms are further defined in the Conference Report. But in view of the Conference Report's statement that "the definitions provided in this Act are generally self explanatory", S. Rep. No. 1126, 95th Cong., 2d. Sess., 69, there is no reason for suggesting that Congress intended to go beyond the normal concept of a sale, as defined in the Uniform Commercial Code as "the passing of title from the seller to the buyer for a price" (U.C.C. §2-106).

Certainly, the inclusion of the words "exchange or transfer for value" in the definition of a sale does not support the court of appeals' opinion. Both terms, in context, connote a transaction involving the transfer of title from a buyer to a seller[23] upon the receipt of appropriate consideration. As long ago as in *Butler v. Thompson,* 92 U.S. (2 Otto) 412, 414-15 (1875), this Court, defining a sale in Blackstone's words as "a transmutation of property from one man to another in consideration of some price," went on to specify that a valid sale in addition to involving a contract or agreement between competent parties, must include "a thing, the absolute or general property in which is transferred from the seller to the buyer" and in addition, "a price in money paid or promised." While the price may be other than money, *e.g.,* an exchange of gas for gas (see U.C.C. §2-304(1)), the need for a transfer of title to goods for consideration remains valid today whether the transaction be labeled a "sale" or a "transfer for value." See *Helvering v. Nebraska Bridge Supply & Lumber Co.,* 115 F.2d 288, 290 (8th Cir. 1940) ("Where a transfer of property takes place without the transferor's receiving anything of value for the property transferred, the transfer is not a sale or exchange."); *Cf. Alexander* v. *FERC,* 609 F.2d 543

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[23]See *Wells* v. *10-X Manufacturing Co.,* 609 F.2d 248, 254, n.3 (6th Cir. 1979) pointing out that Article 2 of the Uniform Commercial Code covers "transactions in goods" which have attributes analogous to a sale but are not sales because their is no transfer of title.

(D.C. Cir. 1979), holding interdepartmental transfer of gas between the Department of the Army and the Defense Family Housing Corporation at Fort Levenworth did not constitute a sale within the meaning of the Natural Gas Act.

As the Commission pointed out (P.A. B-65), throughout the forty years of its administration of the Natural Gas Act, neither it nor any pipeline had ever treated such intracorporate transfers as a sale of natural gas. No certificates had been issued authorizing such "sales" despite the provisions of Section 7(c) of the Natural Gas Act, 15 U.S.C. §717f(c), which make unlawful any sale of natural gas in interstate commerce for resale[24] unless there is in force a certificate of public convenience and necessity.

The Commission also pointed out (P.A. B-66) that since no contracts exist for the imputed sales resulting from the intracorporate transfers, other major consumer protections provided by Section 315 of the NGPA, 15 U.S.C. §3375, would not be available with respect to the pipelines' own production.[25] Moreover, in the absence of any contract for the "sale" limiting the price therefor, the pipeline production would always be eligible for the maximum lawful ceiling rates even where sales by independent producers commanded lower prices as a result of prevailing market conditions reflected in their sales contracts. Of even greater importance, as various categories of a new or high-cost pipeline production became deregulated pursuant to the provisions of Section 121 of the NGPA, 15 U.S.C. §3331, there would be no contractual limitation on the price the pipeline could charge for such deregulated gas.

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[24]Since the alleged sale would be to a "division" of the pipeline for the transportation and subsequent resale along with other "purchased gas," it would clearly fall within the requirements of Section 7 of the Natural Gas Act and would not be exempted by Section 601(a) of the NGPA with respect to gas not committed to interstate commerce as of the effective date of the NGPA.

[25]These provisions govern the duration of gas contracts, *bona fide* offers and rights of first refusal at the termination of such contracts and the right to require that first sale contracts be filed with the Commission.

It is significant in this respect that, while Section 601(b) (1) (E) of the NGPA expressly limits the "just and reasonable" price for a first sale between an interstate pipeline and an affiliate thereof to amounts "paid in comparable sales between persons not affiliated with such interstate pipeline," so such limitation is provided on the lawful price for first sales between divisions of a pipeline. It is, we suggest, apparent that if Congress had consciously intended that intracorporate transfers be classified as "first sales," it would have taken steps to ensure that the charges for such sales as well as those between a pipeline and an affiliate, were no higher than those in comparable arms-length transactions.

It cannot be argued that Congress intended the "Affiliated Entities" provision of Section 601(b) (1) (E) to be applicable to imputed sales *between* internal divisions of an interstate pipeline. Not only does Section 601(b) (1) (E) talk in terms of sales between an interstate pipeline and an affiliate of the pipeline, but the earlier version of the section in the bill which passed the Senate expressly covered both sales between affiliates and pipeline production. See *supra* at 20. This change can only be understood as reflecting a Congressional recognition of the fact that, since the "first sales" covered by the revised bill did not include intracorporate transfers of gas within a pipeline, there was no need to protect consumers against excessive charges for such gas.

The court of appeals' contrary conclusion that Congress intended intracorporate tranfers be classified as "sales" rests on four propositions: (1) the objectives of the NGPA can only be achieved by treating all pipeline production as involving a first sale; (2) the Commission's construction renders nugatory the "unless" clause of Section 2(21) (B); (3) the provisions with respect to pipeline production in Section 203(b) (2) of the NGPA, 15 U.S.C. §3343(b)(2), contemplate that pipeline production involves a first sale; and, (4) language in the Conference Report relating to the Commission's definitional powers also so contemplates. None of these lines of argument can stand analysis.

(1) As pointed out in the Statement, *supra*, the status of pipeline production regulation under the Natural Gas Act when the NGPA was under consideration was that old flowing gas produced from wells drilled before January 1, 1973 on leases acquired before October 8, 1969, which became part of system supply was priced on a cost-of-service basis, whereas most newer pipeline production taken into the system was priced at the analogous rate for sales by independent producers, as was all off-system or wellhead sales of a pipeline's production. The one exception was with respect to a few pipelines who had been specially authorized by the Commission to price their newer production on a cost-of-service basis. There was no suggestion in President Carter's energy message of April 17, 1977, or throughout the lengthy hearings and debates on the various bills which led to the NGPA, that the existing rate treatment of pipeline production by the Commission had in any way inhibited optimum pipeline production efforts, or that departure from the cost-of-service pricing of old gas would in any way serve the public interest. Significantly, none of the pipeline petitioners below so contended. As noted, *supra*, since cost-of-service pricing provides for recovery of all production costs, plus a reasonable return, regardless of the success of the venture, no such claim would have been supportable. Consequently, there is no basis for the court of appeals' surmise that Congress must have intended that pipelines be afforded higher ceiling rates for their cost-of-service production.[26]

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[26]It was not necessary to define all pipeline production as a "first sale" in order to ensure that pipeline production then priced at the levels fixed by the Commission for sales by independent producers would be able to secure the higher NGPA prices. The Commission retained jurisdiction under the Natural Gas Act to equate the price for new pipeline production to that authorized for first sales by independent producers if it concluded that such prices were required. It has in fact done so in Order No. 98 (P.A. B-19). However, the Commission was also in a position to provide in Order No. 98 that pipeline production given NGPA rate treatment pursuant to the exercise of the Commission's discretion under the Natural Gas Act, would, consistent with the restrictions on affiliated production in Section 601(b)(1)(E) of the NGPA, be limited to the prices paid in comparable sales between parties not affiliated with the pipeline (P.A. B-47).

Nor is there merit to the court of appeals suggestion (P.A. A-9 A-10) that requiring the imputation of a sale to intracorporate transfers of all gas produced by interstate and intrastate pipelines and local distributors was essential to avoid the reinstitution of the dual regulatory system whose abolition was one of the NGPA's primary objectives. There is nothing in the legislative history of the NGPA which indicates that cost-of-service pricing of interstate pipeline production by the Commission, or the regulation of intrastate pipeline or local distributor production by state regulatory commissions, had led to the diversion of gas to or from the interstate market. The dual market issue to which the Congress addressed its attention stemmed from the absence of federal regulation over direct or intrastate sales by independent producers which had resulted in much of their gas being diverted from the interstate markets. There was, and is, no reason to believe state regulation of the prices intrastate pipelines or local distributors could secure for their gas would create a significant dual market in the unlikely case they fixed the price for such gas at levels in *excess* of the NGPA ceiling rates. Moreover, if such action in fact led to diversion of significant gas volumes from the interstate market, Section 2(21) (A) (v) of the Act, which is *not* subject to the limitations of subsection (B), authorizes the Commission to classify the subsequent sale of such gas as a "first sale" in order to prevent circumvention of the maximum lawful prices established by the Act.[27]

(2) The court's suggestion that intracorporate transfers must be characterized as first sales in order to give the unless clause of Section 2(21) meaning is simply another facet of the court's improper assumption that Congress, though it did not say so, intended to modify the nature of the Commission's regulation of pipeline production operations under the Natural Gas Act, as well as the pricing of sales of gas by producers to the pipelines. The Commission's interpretation of Section 2(21) leaves the regulation of pipeline production as it was before the adoption of

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[27]Any suggestion that the first sale definition was intended to preclude all differentials between the unit rates charged for gas throughout the nation is negated by Section 602(a) of the NGPA, 15 U.S.C. §3432(a), which expressly authorizes the states to fix lower prices for first sales of gas produced in the state.

the NGPA. Only discrete off-system sales of pipeline production to third parties would be classified as first sales and pipeline production operations which serve to augment system supply would remain under the National Gas Act, with the Commission exercising continuing discretion as to whether such gas should be priced on a cost-of-service basis or allowed a price analogous to the NGPA ceilings. The fact that the portion of the pipeline production qualifying as first sales will be relatively small does not make the Commission's interpretation unacceptable. On the contrary, it is the court's interpretation which strains the language of the Act. For if the normal intracorporate flow of pipeline production results in a first sale, *all* pipeline production will be priced as a first sale. If this was Congress' intent it would have said so, rather than expressly limiting the pipeline production which qualifies for first sale treatment to that which is the subject of a sale "attributable to volumes of natural gas produced by such interstate pipeline ... ".

(3) No support for the court's opinion can be found in the language of Section 203(b) (2) of the NGPA which authorizes the Commission to determine the "first sale acquisition cost" of gas produced by an interstate pipeline or an affiliate thereof for purposes of implementing the incremental pricing provisions of Title II of the Act. To the extent the section is relevant, it reinforces the Commission view that most pipeline production does not involve a first sale.

The twofold objective of Title II of the NGPA was to reinforce market pressures on the pipelines to keep down the prices they contracted to pay producers for gas by allocating a greater percentage of high priced gas purchases to specified industrial users able to utilize alternate fuels, while simultaneously cushioning the impact of price increases upon residential and small commercial users.[28] Incremental pricing was, however, not limited to pipeline purchases of natural gas in first sales subject to Title I. Instead, it applied to all of an interstate pipeline's gas cost above specified levels. See Section 203(a), 15 U.S.C. §3343(a). Since those levels were stated in terms of "first sale acquisition costs," it was necessary to specify what they were for gas not the

[28]See "Explanation Statement" by Congressman Dingell, 124 Cong. Rec. H 13,120 (daily ed. Oct. 14, 1978).

subject of first sales. This was accomplished in Section 203(b)(1)(B) for natural gas or liquified natural gas imports (which are not first sales) in terms of the price paid for the gas at the port of entry to the United States. For pipeline production, however, there was normally no unit cost sale price to which the incremental pricing threshold and passthrough provisions of Sections 203(c) and 204 could be applied. Section 203(b)(2), accordingly, authorized the Commission to determine the "first sale acquisition cost" by rule.

Contrary to the opinion below (P.A. A-11), this provision clearly does not contemplate that all pipeline production would be first sales. The "first sale acquisition cost" for any first sale is defined in Section 203(b)(1)(A). It was only because Congress recognized that most pipeline production would *not* fit into the first sale classification that Congress found it necessary to direct the Commission to adopt rules determining the "first sale acquisition cost" of this portion of its gas supply.[29] If, as the court below believed, all pipeline production fell within the definition of a "first sale," there would have been no necessity for Section 203(b)(2) since the first sale acquisition price for the gas would already have been fixed by Section 203(b)(1).

(4) Finally, no support for the court of appeals' conclusion that "Congress both intended to afford pipeline production first sale status and contemplated that the intracorporate transfer would be treated as a first sale" (P.A. A-11) can be found in the

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[29]Consistent with its position in Order Nos. 58, 98 and 102, the Commission had previously specified that a "first sale acquisition cost" would be "imputed" to pipeline produced gas only where it is "acquired by the pipeline in a transaction which is treated as a first sale for purposes of Title I of the NGPA." See Section 282.303(c) of the Commission's Regulations, 18 C.F.R. §282.303(c). It also made clear in §282.301(k), 18 C.F.R. §282.301(k), that the pipeline production to which a first sale acquisition cost would be imputed would be gas priced in the pipeline's cost of service "without regard to the cost of producing the gas," and that pipeline production "which is treated, for rate purposes, on a cost-of-service basis and which is not acquired by the interstate pipeline in a first sale shall not be subject" to incremental pricing.

language set out on page 116 of the Conference Report which, in discussing the Commission's general authority to define terms pursuant to Section 501(b) of the NGPA, 15 U.S.C. §3411(b), states that "the Commission may define terms such as 'transfer for value' used in the definition of first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition." Since this language does not refer to pipeline production, does not state how the Commission is to exercise its authority and, is written in permissive rather than mandatory terms, it clearly does not express any position as to what Congress "intended" or "contemplated" the Commission would do with respect to treating pipeline production as a first sale.

The Commission, in Order No. 58, assumed that the Conference Report language gave it the permissive authority to classify the transfer of gas within a pipeline as a first sale, but chose not to do so (P.A. B-5). We have considerable doubt as to whether the Commission could lawfully be authorized by any language in the Conference Report to classify as a "transfer for value" falling within the definition of "sale" in Section 2(20)[30], an intracorporate transfer of gas which is not the subject of any contract or agreement, does not affect the title to the gas, and involves no flow of consideration from the imputed buyer to the imputed seller. While statements in conference reports on legislation may be used to clarify the meaning of a statute, they cannot provide independent authority to the agency to expand the coverage of the statute.

However, even assuming *arguendo* that the general language of the Conference Report was directed to the issue presented in this case and could authorize the Commission to interpret the term "transfer for value" in a manner which ignores the last two words and all conventional interpretations of the term, it clearly did not mandate any such action. At most, it authorized the Commission in its descretion to determine that some or all of the gas produced by interstate or intrastate pipelines, local distributors or affiliates thereof, which might normally

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[30]The Conference Report statement is, of course, in error in indicating that the term "transfer for value" is used in the statutory definition of first sale.

not fall within the definition of a "first sale," should be so classified by imputing a prior sale to some intracorporate transaction. Moreover, the Conference Report statement in suggesting additional action the Commission might take under its authority to define terms necessarily assumes that no such interpretation was compelled by the NGPA itself. And, the cited Conference Report language expressly adverting to the Commission's rulemaking authority with respect to the first sale definition shows that the Congress, unlike the court of appeals, was prepared to give deference to the Commission's expertise in this area.

In sum, none of the reasons advanced by the court for requiring the Commission to impute a sale to the intracorporate transfer of gas within the pipeline is valid and the Commission's contrary determination, if not compelled by the language of the Act, was well within its discretion.

IV.

There Is No Valid Basis For Construing Section 2(21) Of The NGPA As Imputing A Separate First Sale To The Portion Of The Subsequent Sale From A Pipeline's System Supply Of Gas Representing Its Own Production

As we have demonstrated, there is no basis for imputing a "first sale" of natural gas to the intracorporate transfer of gas within a pipeline prior to its becoming an undifferentiated portion of the gas supply transported and sold to the pipeline's customers. The "unless clause" of Section 2(21) likewise cannot properly be construed as though it read "unless such sale is attributable, *in whole or part,* to volumes of natural gas produced by such interstate pipeline ... " since this would make all subsequent sales by pipelines with their own production "first sales" and preclude inclusion in the charges for such sales all pipeline costs for transportation and storage of gas from the point of acquisition to the point of delivery to their customers.[31] There remains only to

[31]It would also make impossible any importation of gas at prices in excess of the applicable Title I ceiling prices. Present border prices established by the Mexican and Canadian governments for the substantial volumes of natural gas currently being imported to the United States are well in excess of the analogous "first sale" ceilings.

be considered whether there is any merit to the arguments made by a number of the pipelines below that the NGPA could and should be interpreted as requiring that a first sale be imputed to the portion of the gas included in pipeline sales to their customers that constitutes gas produced by the pipeline itself, even though the only actual sale is not itself a "first sale" within the meaning of Section 2(21).[32]

The arguments by the pipelines in favor of such a construction of the NGPA are almost entirely limited to contentions that Congress intended to make all gas production within the United States subject to the Title I ceiling rates and that any interpretation of the Act which does not achieve this asserted objective is necessarily invalid. We have demonstrated above why these arguments lack merit and will not repeat them here. There simply is nothing in the NGPA or its legislative history which suggests any dissatisfaction with the regulation of pipeline production under the Natural Gas Act or any intent to accord pipeline producers of gas windfall profits aggregating in the millions of dollars each year for the portion of their production which (unlike the gas sold by separate production companies) has been afforded the security of cost-of-service pricing. The most that the pipelines can point to are general statements by the sponsors of the bill that a uniform national pricing system for wellhead sales of natural gas was contemplated, statements which beg the question of what was intended by limiting the ceiling rates prescribed by Title I of the Act to "first sales."

Even if, contrary to the actual situation, there were substantial indicia that Congress consciously intended to accord the first sale ceiling prices to all pipeline production, the language of the Act

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[32]While the court of appeals did not directly pass on such arguments in view of its conclusion that a prior sale meeting the Commission's Attribution Rule could be imputed to the intracorporate transfer of gas, it is clear that this Court can pass upon the question, which is fairly comprehended within the issues upon which certiorari was sought in these consolidated cases. Failure of the Court to resolve the entire issue as to the status of pipeline production under the NGPA would only result in perpetuating uncertainty throughout the industry.

would not permit a construction which achieved such objective by bifurcating the eventual sales of gas by pipelines to their customers into a "first sale" of pipeline production and a simultaneous sale of purchased gas. The separate "sales" assumed by this argument are no less fictitious than the imputed sales resulting from the intracorporate transfer of gas within the pipeline upon which the court of appeals relied. Prior to the adoption of the NGPA, the pipelines never suggested that they were making separate sales to their system customers of purchased gas and gas they had produced, an action which would have required separate certification of the sales under Section 7 of the Natural Gas Act. Nor, throughout the lengthy period the NGPA was under consideration by Congress, was there any pipeline request that any higher new rates which might be prescribed for the gas they purchased from producers for resale should be applied to their own production, to say nothing of proposing that this objective could be accomplished within the context of ceiling rates limited to first sales by imputing separate sales of their own production to their customers. On the contrary, during the period in 1977 and 1978 when the legislation which eventuated in the NGPA was being considered by the Congress, a number of pipelines, including some of the petitioners below, were seeking special permission from the Commission to price their newer production on the same cost-of-service basis that was applicable to their older production on grounds that the certainty of recovering their investment provided by cost-of-service pricing was essential to an optimum production effort. See *Columbia Gas Transmission Corporation*, Opinion No. 74, 20 F.P.S. 5-495 (February 12, 1980); see also *Kansas-Nebraska Natural Gas Company*, 53 F.P.C. 1694, 1696-1698 (1975). It was only when the magnitude of the windfall profits available under NGPA ceiling rates became apparent that the majority of pipeline producers changed their tune.

CONCLUSION

For the foregoing reasons, the opinion below should be vacated and Commission Order No. 58 affirmed. The cases should be remanded to the Court of Appeals for consideration of the objections to Commission Order No. 98 in the light of the Court's opinion.

Respectfully submitted,

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Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301, *et seq.*
Sections 2(20) and 2(21), 15 U.S.C. §§ 3301(20) and (21).

SEC. 2 DEFINITIONS.

***

(20) SALE. — The term "sale" means any sale, exchange or other transfer for value.

(21) FIRST SALE.—

(A) GENERAL RULE.—The term "first sale" means any sale of any volume of natural gas—

(i) to any interstate pipeline or intrastate pipeline;
(ii) to any local distribution company;
(iii) to any person for use by such person;
(iv) which precedes any sale described in clauses (i), (ii), or (iii); and
(v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this Act.

(B) CERTAIN SALES NOT INCLUDED.—CLAUSES (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

Section 101, 15 U.S.C. § 3311.

Section 101. INFLATION ADJUSTMENT; OTHER GENERAL PRICE CEILING RULES

* * *

(b)(9) EFFECT ON CONTRACT PRICE.—In the case of —

(A) any price which is established under any contract for the first sale of natural gas and which does not exceed the

applicable maximum lawful price under this subchapter, or

(B) any price which is established under any contract for the first sale of natural gas which is exempted under Part B of this subchapter from the application of a maximum lawful price under this subchapter,

such maximum lawful price, or such exemption from such a maximum lawful price, shall not supersede or nullify the effectiveness of the price established under such contract.

Section 203, 15 U.S.C. § 3343

Section 203. ACQUISITION COSTS SUBJECT TO PASSTHROUGH

* * *

(b) FIRST SALE ACQUISITION COSTS.—

(1) General rule.—For purposes of this section the first sale acquisition cost of natural gas is—

(A) the price paid, per million Btu's, in any first sale of such natural gas, in the case of any natural gas produced in the United States and acquired in such first sale; and

(B) the price paid for such natural gas, per million Btu's, at the point of entry to the United States, in the case of natural gas or liquefied natural gas imported into the United States.

Any amount of State severance taxes paid at any first sale shall not be included under subparagraph (A) or (B).

(2) Interstate pipeline production.—For purpose of this section, in the case of any natural gas produced by any interstate pipeline or any affiliate of such pipeline, the first sale acquisition cost of such natural gas shall be determined in accordance with rules prescribed by the Commission.

Section 501, 15 U.S.C. § 3411

Section 501. GENERAL RULEMAKING AUTHORITY

(a) In general.—Except where expressly provided otherwise, the Commission shall administer this chapter. The Commission, or any other Federal officer or agency in

which any function under this chapter is vested or delegated, is authorized to perform any and all acts (including any appropriate enforcement activity, and to prescribe, issue, amend, and rescind such rules and orders as it may find necessary or appropriate to carry out its functions under this chapter.

(b) Authority to define terms.—Except where otherwise expressly provided, the Commission is authorized to define, by rule, accounting, technical, and trade terms used in this chapter. Any such definition shall be consistent with the definitions set forth in this chapter.

* * *

Section 601, 15 U.S.C. § 3431

Sec. 601. COORDINATION WITH THE NATURAL GAS ACT

* * *

(b)(1)(E) Affiliated Entities Limitation.—

For purposes of paragraph (1), in the case of any first sale between any interstate pipeline and any affiliate of such pipeline, any amount paid in any first sale shall be deemed to be just and reasonable if, in addition to satisfying the requirements of such paragraph, such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.

Section 602, 15 U.S.C. § 3432

SEC. 602. EFFECT ON STATE LAW.

(a) AUTHORITY TO PRESCRIBE LOWER MAXIMUM LAWFUL PRICES.—Nothing in this Act shall effect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under title I of this Act.

Regulations of The Federal Regulating Commission Under the Natural Gas Policy Act of 1978., 18 C.F.R. §§, 270.101, *et seq*

§270.203 **Pipeline, distributor and affiliate production.**

(a) **Attribution rule for pipelines and distributors.**

For purposes of applying section 2(21)(B) of the NGPA, a sale by a pipeline or distributor is a sale of natural gas attributable to volumes of natural gas produced by such pipeline or distributor to the extent that such sale is comprised exclusively of production volumes of natural gas from identifiable wells, properties, or reservoirs which are owned by such pipeline or distributor.

(b) **Circumvention rule for pipelines and distributors.**

In order to prevent circumvention of the maximum lawful prices established under Title I of the NGPA, the term "first sale" includes any sale by a pipeline or distributor which is comprised of production volumes from identifiable wells, properties, or reservoirs if a portion of those volumes is produced from wells, properties, or reservoirs owned by such pipeline or distributor unless:

(1) the price at which such natural gas is sold is regulated pursuant to the Natural Gas Act or is regulated by a State agency empowered by State statute to establish, modify or set aside the rate for such sale; or

(2) the Commission, on application, has determined not to treat such sale as a first sale.

(c) **Sales by certain affiliates.** Any sale by an affiliate of a pipeline or distributor is a first sale if such affiliate is not itself a pipeline or distributor, unless the Commission, on application, has determined not to treat such sale as a first sale. For purposes of this paragraph, the term "sale" does not include any transaction between an interstate pipeline and an affiliate thereof if such transaction would not have been treated as a sale for purposes of the Natural Gas Act.

(d) **Reports.** A pipeline, distributor or affiliate thereof must file a report with this Commission every 6 months showing the price charged in a sale which was excluded from first sale treatment

under paragraph (b)(2) or (c) of this section. Any determination under paragraph (b)(2) or (c) may be revoked by the Commission on the basis of information in such reports or on the basis of other information.

(e) **Definitions.** For the purposes of this section:

(1) "Pipeline or distributor" means an interstate pipeline, an intrastate pipeline, or a local distribution company.

(2) "State agency" means a State, a political subdivision of a State, or any agency or instrumentality of either.

Supplemental Petitioner's Brief

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IN THE

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OCTOBER TERM, 1982

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*

Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*

Respondents.

On Writ of Certiorari To The Court of Appeals For The Fifth Circuit

MOTION OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK FOR LEAVE TO FILE MEMORANDUM, AND MEMORANDUM ON PRICING OF PIPELINE AFFILIATE GAS PRODUCTION

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MOTION OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK FOR LEAVE TO FILE MEMORANDUM ON PRICING OF PIPELINE AFFILIATE GAS PRODUCTION

The Public Service Commission of the State of New York (New York), the petitioner in Case Number 81-1889, requests leave, pursuant to Rule 35.5, to file the attached Memorandum setting forth its view as to the issue of whether gas produced by producer affiliates of a pipeline and sold to the pipeline was priced upon a cost-of-service basis or received the area or nationwide rates applicable to

independent producer sales during the period the legislation which eventuated in the Natural Gas Policy Act of 1978, 15 U.S.C. §§3301, *et seq.*, was under consideration by the Congress. Since counsel for the petitioners and the respondents made conflicting statements on this matter in response to questions by the Court, it is submitted that the attached Memorandum will be of assistance to the Court in its consideration of these cases.

Respectfully submitted,

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SUPPLEMENTAL MEMORANDUM OF THE PUBLIC SERVICE COMMISSION THE STATE OF NEW YORK ON PRICING OF PIPELINE AFFILIATE GAS PRODUCTION

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TABLE OF AUTHORITIES

CASES: Pages

City of Chicago v. *FPC*, 458 F2.d 731 (D.C. Cir. 1971) 4

Continental Oil Co., 39 F.P.C. 1034 (1968), *aff'd, sub. nom., Cities Services Gas Co.* v. *FPC*, 424 F.2d 411 (10th Cir. 1968) 3

Just and Reasonable National Rates for Sales of Natural Gas, 54 F.P.C. 3090 (1975) 2

Northern Natural Gas Co., 46 F.P.C. 285 (1971) 3

Panhandle Eastern Pipe Line Co. and PanEastern Exploration Co., 48 F.P.C. 581 (1972) 3

Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738 (1969) 2-3, 4

Pipeline Production Area Rate Proceeding (Phase II), 47 F.P.C. 1523 (1972) 3

STATUTE:

Natural Gas Policy Act of 1978, 15 U.S.C. §§3301, *et seq.* ..... *passim*

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On Writ of Certiorari To The Court of Appeals For The Fifth Circuit

SUPPLEMENTAL MEMORANDUM ON PRICING OF PIPELINE AFFILIATE GAS OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

During the course of oral argument on March 22, 1983 in the above proceedings, counsel for the petitioners and respondents were asked whether natural gas produced by affiliates of the interstate pipelines had been priced on a cost-of-service basis prior to the adoption of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. §§3301 *et seq.* Since the responses of counsel were in conflict, and at least one Justice stated his belief that the answer could be material to the Court's decision, we are filing this

memorandum to provide the Court with a more definitive response to the question. Our inquiries reinforce petitioners' position that, as of the period in which the legislation which eventuated in the NGPA was under consideration in the Congress, there was virtually no gas of any vintage produced by pipeline affiliates and sold either to the affiliated pipeline or to third parties which was being priced on a cost-of-service basis. There was, however, substantial production by the pipelines themselves which was priced on a cost-of-service basis, both from leases acquired prior to October 7, 1969, and in cases where the pipeline had secured special Commission permission with respect to gas on newer leases.

Prior to October 7, 1969, all pipeline production and a considerable percentage of the production by pipeline affiliates sold to the pipeline was priced on a cost-of-service basis. See *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738 (1969).[1] However, both pipeline and pipeline affiliate production sold "off-system" was priced at the area and "in-line" rates then applicable to independent producers. *Id.* at 746. In Opinion No. 568 in the *Pipeline Production Area Rate Proceeding, supra,* the Commission determined that both pipeline production

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[1]A Number of pipeline affiliated producers had been named as respondents to the area rate proceedings in which they had operations. The data base from which the average producer costs had been computed in the Permian Basin proceeding and the other early area rate proceedings had included data "submitted by all larger producers (including pipeline affiliates)," but no data on pipeline production was included at the time. See, *Just and Reasonable National Rates for Sales of Natural Gas*, 54 F.P.C. (3090, 3104 (1975). About two and a half years subsequent to the initiation of the Pipeline Production Area Rate Proceeding in 1964 (31 F.P.C. 1595), the Commission joined a group of pipeline-affiliated producers with the pipeline respondents. 36 F.P.C. 954 (1966). As indicated in the Initial Decision in the Pipeline Production Area Rate Proceeding, some of those affiliates, particularly those selling most of their gas to their affiliated pipeline, were then being priced on a cost-of-service basis, while others were not and had been treated like independent producers. See 42 F.P.C. at 779-785, 802, 807.

from leases acquired after the date of the Commission's decision and pipeline affiliate production sold to their pipeline affiliates from newly acquired leases would henceforth be priced at the area rates established for independent producers. Opinion No. 568 did not, however, resolve the pricing problem with respect to either pipeline production, or pipeline affiliate production sold to the pipeline from pre-existing leases. Recognizing that this question "involves separate problems relating to the historical context under which such production efforts were undertaken which by no means necessarily call for the same resolution to be given to future production from leases acquired after, and in the light of, this decision," the matter was reserved to what was then scheduled as Phase II of the "Pipeline Production Area Rate Proceeding." 42 F.P.C. at 746.

The Phase II proceedings were, however, never held. Instead, the Commission on June 14, 1972 issued a brief order terminating the proceedings and stating that the determination of how production from older leases was to be priced would be determined on a case-by-case basis. *Pipeline Production Area Rate Proceeding (Phase II)*, 47 F.P.C. 1523 (1972). In fact, pipeline production on old leases continued in all cases[2] to be priced on a cost-of-service basis. Production by pipeline affiliates from old leases was, in virtually all cases, subsequently priced at the governing area of nationwide rates like the production of independent

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[2]In several situations, where pipelines were authorized to spin-off production properties involving pre-1969 leases to newly organized affiliates, the latter were authorized to charge the pipelines the area or nationwide rates available to independent producers in return for pledges to invest specified sums in additional production efforts. See *Panhandle Eastern Pipe Line Co. and PanEastern Exploration Co.*, 48 F.P.C. 518 (1972), *Northern Natural Gas Co.*, 46 F.P.C. 285 (1971); *Cf. Continental Oil Co.*, 39 FPC 1034 (1968) *aff'd, sub nom., Cities Services Gas Co.* v. *FPC*, 424 F.2d 411 (10th Cir. 1968).

producers, regardless of whether the gas was sold "off-system" to parties unaffiliated with the pipeline affiliate or to the affiliated pipeline itself.[3] There are, to the best of our knowledge, no published orders reflecting this fact. It is memorialized by the absence of any proceeding subsequent

[3]Footnote 20 in the opinion in *City of Chicago* v. *FPC*, 458 F.2d 731 (D.C. Cir. 1971), cited in respondents' briefs for the proposition that sales by pipeline affiliates are priced on a cost-of-service basis, is not to the contrary. It refers to the situation at the time of the Commission's Opinion No. 568 in *Pipeline Production Area Rate Proceeding (Phase I), supra*, which was under review in the *City of Chicago* case, and correctly notes that as of that time some, but not all, of pipeline affiliate gas production was being priced on a cost-of-service basis. It does not discuss the very different situation with respect to the pricing of production by pipeline affiliates on old leases subsequent to the termination of the Phase II proceedings.

to 1969 in which the cost-of-service of any pipeline affiliate production of any vintage was determined either after hearing or by way of settlement.

Respectfully submitted,

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OF THE STATE OF NEW YORK

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Petitioner's Brief

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Nos. 81-1889, 81-1958,
81-2042 and 82-19

IN THE

Supreme Court of the United States

October Term, 1982

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK; ARIZONA ELECTRIC POWER COOPERATIVE, INC.; STATE OF MICHIGAN; AND FEDERAL ENERGY REGULATORY COMMISSION,
Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

**ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT**

BRIEF FOR PETITIONER ARIZONA ELECTRIC POWER COOPERATIVE, INC.

No. 81-1958

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QUESTIONS PRESENTED

1. Whether the Court below erred in holding that intracorporate transfers of gas produced by federally or state regulated pipelines, gas distributors or end users, are "first sales" under the Natural Gas Policy Act of 1978, which must be priced at the maximum ceiling prices of that Act rather than at lower cost of service, area or national rates.

2. Whether the Court below erred in holding that the Natural Gas Policy Act of 1978 terminated, as to all "first sales," the pricing authority of the Federal Energy Regulatory Commission under the Natural Gas Act, so that vacation, rather than remand, was proper with respect to an agency rule setting forth its policies under the latter Act.

PARTIES BELOW

American Gas Association
Anza Electric Cooperative, Inc.*
Arizona Electric Power Cooperative, Inc.
Ciba-Geigy Corporation
Clarke-Mobile Counties Gas District
Colorado Interstate Gas Company
Columbia Gas Transmission Corp.
Conecuh-Monroe Gas District
Consolidated Gas Supply Corp.
Delvan Development Corp.
Duncan Valley Electric Cooperative, Inc.*
Ecee, Inc.
El Paso Natural Gas Company
The Federal Energy Regulatory Commission
Graham County Electric Cooperative, Inc.*
Kansas-Nebraska Natural Gas Company
Kansas State Corporation Commission
Kentucky-West Virginia Natural Gas Company
Michigan-Wisconsin Pipe Line Company
Mid-Louisiana Gas Company
Mobile Gas Service Corp.
Mohave Electric Cooperative, Inc.*
Natural Gas Pipeline Co. of America
Northern Natural Gas Company
Northwest Pipeline Corp.
The Public Service Commission of the State of New York
The Public Service Commission of Wisconsin
The State of Michigan and the Public Service Commission of Michigan
Scotch Plywood Co. of Alabama
Southern Natural Gas Company
Sulphur Springs Valley Electric Cooperative, Inc.*
Trico Electric Cooperative, Inc.*
United Gas Pipe Line Corp.
Wallace Energy Corp.

*Member cooperatives of Arizona Electric Power Cooperative, Inc.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
PARTIES BELOW	ii
TABLE OF CONTENTS	iii
TABLE OF AUTHORITIES	v
OPINIONS AND ORDERS BELOW	1
JURISDICTION	2
STATUTES INVOLVED	2
STATEMENT OF THE CASE	2
SUMMARY OF ARGUMENT	8
ARGUMENT	14
I. THE COURT BELOW UNLAWFULLY REPEALED BY IMPLICATION THE COMMISSION'S NGA JURISDICTION OVER PIPELINE PRODUCTION	14
A. The Court Erroneously Extended The Limited NGPA Repeal Of NGA Gas Pricing Authority To Include Pipeline Production	14
B. The Court Of Appeals Erred In Implying A Repeal Without Any Evidence Of Legislative Intent Or Any Showing That Irreconcilable Differences Exist	20
C. Past Congressional Action In Expressly Repealing The Commission's Powers Over Pipeline Production Makes It Most Unlikely That Congress Repealed the NGA By Implication In The NGPA	22
D. The Court Below Ignored The Pertinent Legislative History Of The NGPA Which Shows That Congress Did Not Intend To Deregulate Pipeline Production	25
E. The Judicial Repeal by Implication Made by The Court Below Produces Inequitable Results	27
II. THE COURT BELOW ERRED IN HOLDING THAT AN INTRACORPORATE TRANSFER IS A "SALE" UNDER THE NGPA	29

III. THE COURT BELOW INTERPRETED SECTION 2(21), THE STATUTORY DEFINITION OF A "FIRST SALE," IN A MANNER WHICH DEPRIVES IT OF ALL MEANING 33

IV. THE COURT BELOW ERRED WHEN IT USED PERIPHERAL HISTORY OF THE NGPA TO SUPPORT IS VIEW 36

A. The Legislative History Does Not Support The View That An Intracorporate Transfer Is A First Sale 36

B. The Court Below Applied The Wrong Standard For Judicial Review 38

V. THE COURT BELOW UNLAWFULLY USURPED THE ADMINISTRATIVE FUNCTIONS OF THE COMMISSION IN VACATING ORDER 98 40

CONCLUSION 42

ADDENDUM ..... A-1 — A-15

TABLE OF AUTHORITIES

CASES **Page**

Addison v. Holly Hill Fruit Products, 332 U.S. 607 (1944) 17

Banks v. Chicago Grain Trimmers Ass'n, 390 U.S. 459 (1958) 17

Burns v. Alcaa, 420 U.S. 575 (1975) 17

Colorado Interstate Gas Co. v. FPC, 324 U.S. 581 (1945), affirming *In re Canadian River Gas Co.,* 3 FPC 32 (1942) 3

Columbia Gas Development Corp. v. FERC, 651 F.2d 1146 (5th Cir. 1981) 21

Commissioner of Internal Revenue v. Brown, 380 U.S. 563 (1965) 9, 17, 32

Democratic Central Committee v. WMATC, 485 F.2d 786 (D.C. Cir. 1973) 29

FCC v. Pottsville Broadcasting Co., 309 U.S. 134 (1940) 41

FPC v. Idaho Power Co., 334 U.S. 17 (1952) 13, 41

Georgia v. Pennsylvania Railway Co., 324 U.S. 439 (1945) 21

Just and Reasonable National Rates for Sale of Natural Gas, 51 FPC 2212 (1974), *aff'd sub nom., Shell Oil Co. v. FPC,* 520 F.2d 1061 (5th Cir. 1976), *cert. denied, sub nom., California Co. v. FPC,* 426 U.S. 941 (1976) 4

Morton v. Mancari, 417 U.S. 535 (1974) 18, 21

National Coal Operators Ass'n v. Kleppe, 423 U.S. 388 (1976) 27

National Rates for Jurisdictional Sales of Natural Gas, 56 FPC 509 (1976), *aff'd sub nom., American Public Gas Association v. FPC*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978) 3

National Small Shipments v. CAB, 618 F.2d 819 (D.C. Cir. 1980, ... 37

Neal v. Scruggs, 95 U.S. 704 (1878) 30

Permian Basin Area Rate Proceeding, 34 FPC 159 (1965), *aff'd, Permian Basin Area Rate Cases*, 390 U.S. 747 (1968) 3

Perrin v. U.S., 444 U.S. 37 (1979) 17

Phillips Petroleum C. v. Wisconsin, 347 U.S. 672 (1954) 3

Pipeline Production Area Rate Proceeding, 42 FPC 738 (1969), *aff'd sub nom., City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972) 4, 35

Posades v. National City Bank, 296 U.S. 497 (1936) 21

Russell Motor Car Co. v. U.S., 261 U.S. 514 (1923) 32

Securities and Exchange Commission v. Chenery Corp., 318 U.S. 80 (1942) 13, 41

Union Electric Co. v. EPA, 427 U.S. 246 (1976) 11. 27

U.S. v. Borden Co., 308 U.S. 188 (1939) 18

U.S. v. Greathouse, 166 U.S. 606 (1897) 25

U.S. v. Great Northern Railway Co., 287 U.S. 144 (1932) . 20

U.S. v. Pfitsch, 256 U.S. 547 (1921) 20

STATUTES

Natural Gas Act, 15 U.S.C. § 717 *et seq.* ..... *passim*
Section 1, 15 U.S.C. 717 ..... *passim*
Section 1(b), 15 U.S.C. 717(b) 14
Section 4, 15 U.S.C. 717c 14, 16
Section 5, 15 U.S.C. 717d 14, 16, 23
Natural Gas Policy Act, 15 U.S.C.§§ 3301 *et seq* ..... *passim*
Section 2(20), 15 U.S.C. 3301(20) 30
Section 2(21), 15 U.S.C. 3301(21) 34-35
Section 2(21) (A), 15 U.S.C. 3301(21) (A) 34
Section 2(21) (B), 15 U.S.C. 3301(21) (B) 35
Section 2(22), 15 U.S.C. 3301(22) 31
Section 501, 15 U.S.C. 3411 38-39
Section 501(a), 15 U.S.C. 3411 (a) 38
Section 501(b), 15 U.S.C. 3411(b) 12, 38-39
Section 601, 15 U.S.C. 3431 ..... 9, 16, 18
Section 601(b), 15 U.S.C. 3431(b) 9, 16, 18
Section 601(b) (1) (A), 15 U.S.C. 3431(b) (1) (A) .9, 16, 18
Section 601(b) (1) (E), 15 U.S.C. 3431(b) (1) (E) 9, 18
Section 601(c) (2), 15 U.S.C. 3431(c) (2) 9, 16
Department of Energy Act, Pub. L. 95-91, August 4, 1977, 91 Stat. 565 2

LEGISLATIVE HISTORY

S. 2104, 95th Congress, 1st Session (1977) 19, 26
H.R. 8444, 95th Congress, 1st Session (1977) 25, 26
H.R. 6645, 84th Congress, 2d Session (1956) 23
H.R. 1758, 81st Congress, 2d Session (1950) 22, 23
S. Rep. 95-1126, 95th Congress, 2d Session (1978) 30
H.R. Rep. 95-543, Volume II, 95th Congress, 1st Session (1977) 25
H.R. Rep. 84-992, 84th Congress, 1st Session (1956) 24

REGULATIONS

Order No. 58, Docket No. RM80-7, (issued November 14, 1979) 14
Order No. 98, Docket No. RM80-6, (issued August 4, 1980) 28, 40-41
Order No. 102, Docket Nos. RM80-6 and RM80-7, (issued October 3, 1980) 28-29
18 C.F.R. 2.66(a) (4) 5, 7
18 C.F.R. 270.203(a) 6

MISCELLANEOUS

Black's Law Dictionary, 5th Edition 30-31
House Rule XXVIII.3. 26-27
Jefferson's Manual, Section 546 27

Nos. 81-1889, 81-1958,
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**BRIEF FOR PETITIONER
ARIZONA ELECTRIC POWER COOPERATIVE, INC.**

OPINIONS AND ORDERS BELOW

The opinion of the United States Court of Appeals for the Fifth Circuit is reported at 664 F.2d 530,and is reprinted in Appendix A.[1] The Commission's Order Nos. 58, 59 and its Order on Rehearing, No. 102, are not reported and are set out in Appendix B.

[1]By agreement of the parties and with the concurrence of the Court, no "Joint Appendix" will be prepared in this case. Instead, the parties will use the Appendix to the Petition for Certiorari of the Public Service Commission of the State of New York which contains most of the pertinent decisions, orders and statutes. That Appendix will be cited hereinafter as (App. _____). AEPCO includes at the end of this brief addenda to that appendix. References to the Addenda will be hereinafter given as "(Add. _____)".

JURISDICTION

The judgment of the United States Court of Appeals for the Fifth Circuit was entered on December 23, 1981 (App. C-1). On January 11, 1982, the Court extended the time for petitions for rehearing until January 20, 1982 (App. C-2). Petitions for rehearing en banc filed by AEPCO and the State of Michigan and the Public Service Commission of Michigan, and for rehearing filed by the Public Service Commission of the State of New York, were denied on February 5, 1982 (App. C-3). This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

STATUTES INVOLVED

The Statute upon which the Court of Appeals decision is based is the Natural Gas Policy Act of 1978, 15 U.S.C. §§3301, *et seq.*, the relevant portions of which appear in Appendix D and Addendum C.

STATEMENT OF THE CASE

In 1938, Congress enacted the Natural Gas Act (NGA), 15 U.S.C. 717, *et seq.* which gave the Federal Power Commission (FPC)[2] authority to regulate rates for natural gas sold by interstate pipelines. Such pipelines purchase or produce natural gas, transport it through interstate pipelines, and sell it at wholesale to resale gas distributors or at retail to direct industrial customers.

Historically, most natural gas transported by interstate pipelines was purchased from independent producers. The FPC permitted the pipelines to pass through to their customers the cost of purchased gas. However, many of the major interstate pipelines produced significant quantities of gas from properties which they owned or controlled. Most of this gas was used "on system" to serve the pipelines' own customers, although some pipeline produced gas was sold at the wellhead to other pipelines

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[2]The functions of the Federal Power Commission were transferred to the Federal Energy Regulatory Commission (Commission) in 1977 by the Department of Energy Act, Pub. L. 95-91, Aug. 4, 1977, 91 Stat. 565.

or end users which were not regular customers of the pipeline. These are "off-system" sales.

From the beginning of federal regulation under the NGA, rates of interstate pipelines were established on a "cost of service" basis. Under this method, pipelines recover all operating expenses, depreciation, taxes, and a fair return on investment from their customers. The pipeline's rates are determined by dividing total costs by the volume of gas produced. No unit rate, per Mcf or MMBTU,[3] was ever set for gas produced by the pipeline for use by its own customers. *Canadian River Gas Co, et al.*, 3 FPC 32 (1942), *aff'd sub nom., Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945). The costs associated with exploration, development and production are included with all other items in the cost of service and are an element in the final rate. Under the cost of service method, pipelines recover these exploration and development costs irrespective of the ultimate cost of the natural gas or whether these efforts are even successful. Thus, the entire risk of a pipeline's exploration and development program is borne by its customers and they pay only the actual cost whether it is above or below the price charged by independent producers.

In *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954), this Court determined that under the NGA, the FPC also had jurisdiction over the prices charged to interstate pipelines by independent producers. Following *Phillips*, the Commission initiated several proceedings to determine the maximum prices which independent producers could charge. *Permian Basin Area Rate Proceeding*, 34 FPC 159 (1965), *aff'd, Permian Basin Area Rate Cases*, 390 U.S. 747 (1968); *National Rates for Jurisdictional Sales of Natural Gas*, 56 FPC 509 (1976), *aff'd sub nom. American Public Gas Association* v. *FPC*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978). In fixing these prices, the Commission established cost related maximum *unit* rates, first on an area and then on a national basis. Such rates

[3]An Mcf is a thousand cubic feet of natural gas. An MMBTU is a million British thermal units. The heating value of one Mcf is approximately one MMBTU.

were geared to *average* producer costs. In addition, if the producer's cost exceeded the average, he would not earn a fair return on his investment and his stockholders would bear the loss. If he was more successful than the average, he realized greater profits.

In the *Pipeline Production Area Rate Proceeding* (Phase I), 42 FPC 738, (1969), *aff'd sub nom., City of Chicago* v. *FPC, 458* F.2d 731 (D.C. Cir. 1971), *cert. den.*, 405 U.S. 1074 (1972), the FPC found that interstate pipeline production should enjoy parity of pricing with independent producers but only with respect to leases acquired after October 8, 1969 — the date of its decision. Producing wells on leases acquired prior to that date would continue to be treated on a cost of service basis, *as would future wells on these leases.* Production from leases acquired after that date would receive the same treatment as production by independent producers, *i.e.*, the applicable area or national unit rate. Thus, on leases acquired after the Commission's decision, the pipelines would assume the risk of loss in the same manner as independent producers.

Because of the acute gas shortages and extensive curtailments on most pipeline systems in the mid-1970s, the FPC also gave the higher area or national rates to pipeline producers on old leases as an inducement to drill more wells on leases which would otherwise have received cost of service treatment. Thus, in *Just and Reasonable National Rates for Sale of Natural Gas,* 51 FPC 2212 (1974), *aff'd sub nom., Shell Oil Co.* v. *FPC,* 520 F.2d 1061 (5th Cir. 1976) *cert.den., sub nom, California Co.* v. *FPC,* 426 U.S. 941, (1976), the FPC determined that production from wells completed after January 1, 1973 on leases acquired prior to October 8, 1969, would also be eligible for area or national rates. *The FPC did this in a manner which insured that the pipelines would always be given the higher of cost of service rates or area or national rates.* Thus, on a case-by-case basis, the FPC granted cost of service treatment for any production or portions thereof if the pipeline could "show in a rate proceeding that special

circumstances exist which justify different treatment" (18 CFR 2.66(a)(4)). These special circumstances were that the applicable area or national rate was *less* than the cost of service rate. In addition, pipelines could obtain cost of service treatment for new properties through a settlement agreement with their customers. The Commission approved several such agreements.

In 1978, the Natural Gas Policy Act (NGPA) was enacted as compromise legislation after extensive deliberation. The NGPA established a scheme of maximum price ceilings for different categories of natural gas. It provided that some categories were to remain permanently subject to regulation and others were to be deregulated on a fixed time schedule beginning on January 1, 1985.[4] Congress specified different prerequisites for eligibility for the ceiling price in each of the respective NGPA categories of natural gas. However, the existence of a statutory "first sale" is a common and indispensable prerequisite for eligibility for any NGPA price. Section 2(21)(A) specifies that a first sale means any volume of natural gas sold *to* an interstate or intrastate pipeline, a local distribution company or a direct gas consumer. Section 2(21)(B) specifically excludes from the scope of a statutory "first sale" the sale of any volume of gas *by* an interstate pipeline, intrastate pipeline or local distribution company or affiliate thereof "unless such sale is attributable to volumes of natural gas produced" by such a seller. The Court below held that the legislative history of Section 2(21) does not shed any light on its intended meaning:

> Congress did not explain its definition of first sale either in the Committee reports that accompanied the various drafts of the NGPA or in the discussions that occurred in each House. [App. A-10].

In Order 58, acting pursuant to its NGPA authority under Section 501(a) to make substantive rules and its authority under Section 501(b) to define terms, the Commission interpreted

[4]Certain categories of "high cost" gas have already been deregulated.

Section 2(21) as excluding from the definition of first sale, the intracorporate transfers of gas from a pipeline's production division to its transmission division. The agency relied on the "unless" clause of Section 2(21) and upon the literal language of that provision which required "that a sale be 'attributable' to the pipeline's own production" (App. B-3). Under this ruling, as the Commission expressly noted, "if a pipeline were to sell its production at the wellhead, in an offsystem sale, such a sale would generally qualify under 18 C.F.R. 270.203(a) as a first sale." (App. B-2).

The Commission held that NGPA maximum ceiling prices should be applied to actual sales rather than to *bookkeeping and accounting entries of a corporation.* On rehearing, the five pipeline petitioners below[5] urged the Commission to impute a sale at the point at which the pipeline takes its production into its general system supply. The Commission held that it had discretionary authority to do this under Section 501 of the NGPA and thereby accord first sale treatment to pipeline production (App. B-65). However, it stressed that its authority was *discretionary* (App. B-65) and noted that in its administration of the NGA, it had never treated such an intracorporate transfer as a sale. It relied on the facts that no contracts govern such transfers; no certificates under the NGA were issued or required for such transfers; and treating such transfers as sales could not be reconciled administratively with certain provisions of the NGPA.

In Order 98, the Commission determined that since pipeline production which was the subject of an intracorporate transfer was not a "first sale," it was called upon to exercise its discretionary powers under the NGPA to determine whether pipeline production which had received area or national rates under the NGA should continue to receive such rates or should be made eligible for NGPA prices. The Commission thus extended

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[5]Mid-Louisiana Gas Co., Kansas-Nebraska Natural Gas Co., Michigan-Wisconsin Pipe Line Co., Consolidated Gas Supply Corp. and Kentucky-West Virginia Natural Gas Co.

its parity of rate treatment policy by granting NGPA prices to pipeline production which had been receiving area or national rates under the NGA (App. B-25).

Order 98 also continued the Commission's policy respecting pipeline production by denying NGPA prices to all gas which had ever received cost of service rate treatment. It gave as the reason for this policy the fact that pipeline customers had paid for all exploration and development costs of such properties and equity required that the customers who had borne the risks receive the benefits of these production efforts (App. B-26).

Order 98 applied the same rationale to deny parity of pricing treatment to pipeline producers who had been permitted to depart from the area or nationwide rate and receive a higher cost of service rate under the "special circumstances provisions" of 18 CFR 2.66(a)(4) or a settlement agreement with its customers. It specifically noted that pipelines receiving such treatment had passed the risks of production ventures on to their customers in exchange for assuring those customers the opportunity to enjoy the benefits of successful ventures at a cost of service rate (App. (B-26-27).

Order 102 denied rehearing of both Order 58 and Order 98. This order gave *new and independent* reasons to support Order 58.

In *Mid-Louisiana,* the Fifth Circuit had before it petitions for review of Orders 58, 98 and 102. The Court held that on the basis of "...the language, purposes and history of the NGPA, we hold that Congress clearly intended for any production attributable to an 'interstate pipeline, intrastate pipeline or local distribution company, or any affiliate thereof' to be accorded first sale status under the NGPA and that Congress contemplated that the intracorporate transfer of pipeline production to the pipeline would be treated as the first sale" (App. A-15).

On this basis, the Court held that the Commission had erred in refusing to accord "first sale" status to *all* pipeline produced gas, whether sold on-system or off-system. It therefore vacated Order 58. Since, in its view, the NGPA had terminated all of the Commission's NGA Section 4 and 5 authority over pipeline

pricing, the Court also voided Order 98. It found it unnecessary to consider this latter order on its merits. The Court held that no deference was due to the contrary interpretation of the statute by the Commission because interpretation of the NGPA was not an area where the Commission had any particular expertise, nor had that agency assisted in developing the terms in that Act (App. A-15).

Finally, the Court found that cost of service rate treatment of pipeline production was merely a "continually diminished" exception to area and national rates and stated that this category of gas "does not affect our decision" (App. A-3). The Court did not elaborate further, although in petitions for rehearing of *Mid-Louisiana,* many parties pointed out that cost of service gas constituted a major portion of the gas produced by many pipelines.

The Court did not vacate, reverse, or even mention Order 102 which was the final order of the Commission in the rulemaking proceeding.

SUMMARY OF ARGUMENT

Since its enactment, the NGA has been consistently interpreted to require cost-related pricing of natural gas produced by pipeline. *Colorado Interstate, supra.* Under the NGA, the Commission used two mechanisms to set a just and reasonable rate for gas sold on-system to the pipeline's own customers. First, it directly regulated the price charged for different categories of gas sold at the wellhead or in the field. Second, it regulated the price indirectly by limiting the ability of the pipeline to collect from consumers the amounts paid for gas. The Commission could only lose such dual authority if Congress expressly or implied repealed it.

The NGPA repealed both aspects of this authority with respect to "first sales" of gas, but this repeal was limited to gas produced by independent producers and pipeline production affiliates. The Court below held that Congress intended, by implication, to repeal both aspects of the Commission's NGA authority over *all*

gas produced by pipelines and that a "first sale" at the wellhead must be imputed to the intracorporate transfer of natural gas produced by pipelines.

Repeals by implication are not favored and must be supported by evidence of a "clear and manifest" Congressional intent to repeal, or a showing of an irreconcilable difference between an earlier and later statute. Here, there is *no* evidence of either. In fact, the Court below made no findings on the issue of NGA repeal. Therefore, the Court below clearly erred.

The best evidence of Congressional intent is the *express* and *limited* repeal of NGA powers under Sections 4 and 5 to regulate producers made by the NGPA. Title I of the NGPA establishes ceiling prices for the first sale of various types of gas. Section 601(b) (1) (A) provides that "any amount paid in any first sale of natural gas shall be deemed to be just and reasonable..." if it is equal to or less than the ceiling prices prescribed in Title I. These two provisions effectively terminate the Commission's direct power to set prices for first sales of gas at the wellhead when the sale is made by an independent producer or pipeline production affiliate.

Section 601(c) (2) of the NGPA states that the Commission may not "deny any interstate pipeline recovery of *any amount paid* with respect to *any purchase* of natural gas..." (emphasis added) provided that the NGPA ceiling prices are not exceeded. The operative words in this section are "any amount paid" and "any purchase." Statutory terminology must usually be accorded its "common and ordinary" meaning absent a showing of Congressional intent to the contrary. *Commissioner of Internal Revenue v. Brown,* 380 U.S. 563, 570-571 (1965). The common and ordinary meaning of "any amount paid" and "any purchase" cannot include an intracorporate transfer. No amount is paid for the gas and none of the normal *indicia* of a purchase, *i.e.,* a contract or consideration, are present. One simply cannot purchase something from oneself.

Further, Section 601(b) (1) (E) provides that a pipeline which buys natural gas from its affiliate may not pass through that part

of the purchase price which exceeds the price paid in comparable first sales from non-affiliated producers. There is no similar restriction on pipeline intracorporate transfers, although Congress was well aware (see § 203(b)(2) of the NGPA) that there is an equivalent lack of arms-length dealing in such transactions. The absence of this comparable price test—especially when such a provision was included in S. 2104, the Senate version of the NGPA—is strong proof that Congress *did not intend the NGPA to apply to such pipeline production.* It is absurd that a pipeline which produces gas through a separately incorporated affiliate can charge itself only the price it would pay to non-affiliated producers while a pipeline which elects to conduct its business as a single corporate entity may pay itself a much higher price.

During the 1950s, Congress twice passed legislation which would have deregulated natural gas prices.[6] The 1950 Bill deregulated independent producer production but *specifically* continued regulation of pipeline and affiliate production. The 1956 Bill deregulated all production, *specifically* including pipeline and affiliate production. In addition, the House Report accompanying this latter Bill *specifically* stated an intent to treat pipeline intracorporate and affiliate production in the same manner as independent production. The specific provision Congress has made in the past for pipeline and affiliate production in such bills contrasts strongly with the total silence of the NGPA as to intracorporate pipeline production. This is strong proof that Congress did not intend to repeal the specific powers of the Commission under the NGA over such production.

The legislative history of the NGPA also proves that no repeal of the Commission's NGA powers over pipeline production was intended. The House Bill provided higher prices only to natural gas sold in a first sale. The House Report specifically stated that first sale pricing would be limited to the first "transfer for value" at the wellhead. This obviously excluded pipeline production. The Senate Bill totally deregulated *new* natural gas (*i.e.* gas from reservoirs discovered after January 1, 1977 or from extensions of existing reservoirs discovered after that date) from all sources,

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[6]Both bills were vetoed.

including pipelines, and left old (all other) natural gas subject to NGA regulation.

Thus, the House would have left pipeline production entirely under NGA regulation and the Senate would have left "old" pipeline production under NGA regulation. Neither House proposed total elimination of NGA jurisdiction. Therefore, the conclusion of the Court below that the Conference Committee's compromise bill was intended to apply to both old and new pipeline production necessarily assumes that the Conference Committee exceeded its authority. It is clear that where both Houses provided that regulation of "old" pipeline production under the NGA should continue, the Conference committee could not take broader action, *Union Electric Co.* v. *EPA*, 427 U.S. 246, 262-263 (1976).

Finally, under NGA cost of service pricing, the consumer assumed the entire risk of loss in connection with pipeline production activities whether or not these efforts were ultimately successful. There is a well established principle of utility law that the party which bears the risk of loss is entitled to any gain resulting from that risk. The consumers assumed the entire risk of loss with respect to cost of service reserves, and under this principle they are entitled to the benefits (*i.e.* to buy this gas on a cost-plus basis). The Court below held—without any express support from the statute or its legislative history—that Congress intended to deprive consumers of the benefit of their bargain and do away with this important ratemaking principle.

The Court below based its holding on the novel theory that an intracorporate transfer is a statutory "first sale" because the "...NGPA contemplates that the pipeline is both a buyer and seller as to its own production"(App.A-8). The Court did not cite any statutory text or legislative history to support this view. Furthermore, the Court completely disregarded the crucial fact that the NGPA definition of first sale incorporates the definition of "sale" in Section 2(20). Congress defined the latter term only as a "sale, exchange, or transfer for value." It is plain that the ordinary meaning of this language contemplates a separate buyer and seller, with an exchange of some item for something of value. Here, there is nothing more than a bookkeeping entry by a single corporation and no money or title changes hands.

There is a general rule of statutory construction which requires words in a Federal statute to be given their ordinary meaning. This rule has been specifically applied to the words "sale" and "exchange." The case for using the *ordinary* meaning of words is even stronger here since the Conference Committee stated that the "definitions provided in the Act are generally self-explanatory, except as noted." A definition can only be self-explanatory if the *ordinary* meaning of the words used is intended. Thus, Congress has specifically directed that the crucial term "sale" be construed in a manner which excludes intracorporate transfers.

The Court below evaded the plain language of the NGPA by taking the unusual step of creating a "fictional sale" which it found the Commission *must impute* to every intracorporate transfer of pipeline produced gas. The Court did not cite any text of the statute, or any legislative history, which stated or even implied that its literal definitions were to be perverted in this manner. The Court professed to find some evidence of legislative intent in the Conference Committee Report which stated that "the Commission *may* define terms [and]...*may* also establish rules...". (Emphasis added). But, on its face, this language does not permit the Court to compel the Commission to exercise this discretion—particularly in a specific manner. In so doing, the Court clearly overstepped its authority even if it is correct as to the intent of Congress.

Section 501(b) of the NGPA *authorizes* the Commission "...to define, by rule, accounting, technical, and trade terms used in this Act." Again, the fact that the Commission has *discretion* to make such rules, does not empower a court to direct the Commission to exercise that power in a particular manner. Finally, the Commission was directed by the Court below to define a "first sale" in a manner contrary to the NGPA definition of a "sale."

The Court below erroneously held that the Commission's Order 58 defined a first sale in a manner which nullified the "unless" clause of Section 2(21) (B) of the NGPA. The short answer to this claim is that the Commission has permitted pipelines to receive NGPA first sale ceiling prices for off-system

wellhead sales and even to receive such prices for on-system sales of gas volumes derived from the pipeline's own production so long as the specific source of such volumes is identified by contract. The fact that only a small portion of total pipeline sales qualifies does not nullify the clause.

The remedy which the Court below prescribed for the alleged nullification of the "unless" clause by the Commission was to nullify, in its entirety, the first sale definition. Under the interpretation by the Court below, *all* gas produced in the United States by an interstate or intrastate pipeline, gas distributor or industrial user is eligible for NGPA price ceilings and is completely removed from pricing jurisdiction under Section 4 and 5 of the NGA. If this was the intent of Congress, there was no need to limit NGPA price ceilings to gas sold in a "first sale."

The Court below held that since the Commission had lost all of its authority to set prices for interstate pipeline production under the NGA, those prices would have to set under the NGPA (App. A-15). Order 98 did not set any price or rate for natural gas. Rather, it barred those pipelines which had received cost of service on specific leases from collecting higher NGPA rates on gas produced from them. Neither the Commission nor the Court addressed the question of whether any agency jurisdiction under the NGA would have survived if intracorporate transfers of pipeline production were NGPA first sales (App. B-71). Had the Commission been aware of this loss of gas pricing jurisdiction, it could have written this same order in terms of its surviving NGA powers.

By vacating Order 98 instead of remanding that rule to the Commission for further consideration, the Court usurped the agency's administrative functions. When an agency has acted on the basis of a mistaken legal interpretation, the reviewing court has only the power to uncover the error of law and must remand the case to the agency. *FPC* v. *Idaho Power Co.*, 344 U.S. 17, 20 (1952); *SEC* v. *Chenery Corp.*, 318 U.S. 80, 88 (1942). Therefore, this Court must reverse the action of the Court below in vacating Order 98 even if it affirms as to Order 58.

I. THE COURT BELOW UNLAWFULLY REPEALED BY IMPLICATION THE COMMISSION'S NGA JURISDICTION OVER PIPELINE PRODUCTION

A. The Court Erroneously Extended The Limited NGPA Repeal Of NGA Gas Pricing Authority To Include Pipeline Production

Since 1938, Sections 4 and 5 of the NGA, 15 U.S.C. 717c and 717d, have been uniformly construed to empower the Commission to regulate the just and reasonable rate for gas produced by pipelines and sold "on-system" to their customers. Such regulation has been sustained against arguments by pipelines that Section 1(b) of the NGA exempted production and gathering operations from Commission jurisdiction. Instead, such gas producing operations were held to be an integral part of pipeline total operations, the cost of which must be reflected in the "just and reasonable" rates set by the agency. *Colorado Interstate, supra.*

In Order No. 58, the Commission implemented its view that the NGPA did not affect its powers over pipeline production under the NGA. The Court below vacated this rule, holding that "...the Commission lacked authority to set prices for interstate pipeline production under the NGA ..." (App. A-15). If the Court erred in its pivotal assumption that there has been a total repeal of such NGA powers by the NGPA, its decision vacating Orders 58 and 98 is clearly wrong and must be reversed. We shall demonstrate that there has been neither an express nor an implied repeal of the powers of the Commission under the NGA to regulate the price of pipeline production which is the subject of an intracorporate transfer.

In *Philips Petroleum, supra,* the scope of the Commission's Sections 4 and 5 ratemaking powers over the pricing of natural gas under the NGA was extended to include independent producers as well as pipelines. It was the power to regulate just and reasonable rates for *independent producers* that the NGPA

was intended to repeal.[7] Such limited repeal reflected the awareness of Congress that there was a vast difference between the risks incurred by pipelines and by independent producers in exploring for natural gas.

Traditionally, an independent producer expended funds in the search for additional gas supplies with no assurance that there would be any relationship between the size of its expenditure and the profit it would realize from any additional hydrocarbon reserves discovered. Pipelines, on the other hand, invested funds in their own production knowing that under binding long-term contracts, their customers had assured the recovery by the pipeline of all production and transmission costs. The independent producer was also subject to the vagaries of demand for gas, which is sensitive to both natural and local economic conditions, the price of alternate fuels, weather and a variety of other factors beyond the producer's control. The pipeline, on the other hand, never bore the risk that it would discover gas and be unable to sell it. Finally, the pipeline knew that even if the gas it ultimately produced was uneconomical and exploration had resulted in higher than average costs per unit of gas or, in fact, no gas was discovered, it was still assured full cost recovery under the cost of service method. Producers were understandably reluctant to undertake comparable risks in searching for hard to develop and costly gas supplies unless they were afforded the incentive of higher prices for such supplies than for conventional gas supplies.

For these reasons, Congress expressly repealed the powers of the Commission to fix just and reasonable rates for independent producers and for pipeline production affiliates which incur the same risks as independent producers but continued such powers with respect to the bulk of pipeline production. For the pipeline's customers—not the pipeline—have assumed the entire risk of such production activities under the cost of service method

[7]See Section 401(a)(4) of H.R. 8444, 95th Cong., 1st Sess.—the House verson of the NGPA — which mentions this issue (Add. A-6).

of rate regulation. The express language of the sections of the NGPA which repeal the rate powers of the Commission clearly shows that Congress distinguished between the producer and affiliate risk takers and the risk-free pipelines.

Under the NGA, the Commission had dual jurisdiction over gas production. It could directly set a "just and reasonable" rate to be charged by the producer. Indirectly, it could determine whether to allow the pipeline to increase its own rate to reflect the higher rates paid to a producer. Section 601 of the NGPA expressly repeals both the Commission's direct and indirect powers over gas produced by an independent producer or by a pipeline production affiliate. That section does not, however, repeal any portion of the Commission's powers under the NGA with respect to pipeline production which is the subject of an *intracorporate transfer* rather than of a *sale and purchase*.

Section 601(b) (1) (A)[8] provides that for the purposes of Sections 4 and 5 of the NGA " ... any amount paid in any first sale of natural gas shall be deemed to be just and reasonable ... " if it is equal to or less than the applicable NGPA ceiling price. Thus, Congress has expressly repealed, in its entirety, the Commission's statutory power under the pertinent sections of the NGA to determine "just and reasonable" rates for gas which is the subject of a "first sale."[9] But, as shown below (pp. 29-33) there is no "sale" and, therefore, no "first sale" in an intracorporate transfer. Therefore, the Commission has retained its statutory authority under the NGA to fix rates for such pipeline production.

Sections 601(c)(2), "Recovery of Just and Reasonable Prices Paid,"[10] expressly repeals the Commission's authority under NGA Sections 4 and 5 to " ... deny any interstate pipeline recovery of *any amount paid* with respect to *any purchase* of natural gas ... " (emphasis added) provided that the amount at issue meets the just and reasonable test of Section 601(b). Clearly, the operative words in this section are "any amount paid" and

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[8]Addendum C. p. A-15, for text of §601(b)(1)(A).

[9]See discussion *infra*, pp. 33-36.

[10]See Add. C. p. A-15, for text.

"any purchase." There can be no question that there is neither an "amount paid" nor a "purchase" in an intracorporate transaction. The pipeline makes, at most, a bookkeeping entry; no money changes hands and no title passes. In short, a party cannot purchase from itself something it already owns.

Furthermore, in *Commissioner of Internal Revenue* v. *Brown*, 380 U.S. 563, 570-571 (1965), the Court held that when terms are used in a statute " ... without limiting definition and without legislative history indicating a contrary result, [the] common and ordinary meaning should at least be persuasive of its meaning..."[11] Therefore, these crucial words must be interpreted in light of their ordinary meaning since the NGPA does not define either the term "amount paid" or the term "purchase" and the legislative history does not indicate a contrary intent. In *Brown*, the Court used other statutes of general application, *e.g.*, the Uniform Commercial Code, to determine the ordinary meaning of terms used in federal statute. Applying this practice, Section 1-201(32) of the Uniform Commercial Code defines the term "purchase." It states:

> "Purchase" includes taking by sale, discount, negotiation, mortgage, pledge, lien, issue or re-issue, gift or any other voluntary transaction creating an interest in property.

Such formal indicia of a bona fide transaction between separate legal entities is clearly and totally lacking in the case of an intracorporate transaction.

Congress carefully and precisely repealed the power of the Commission to set just and reasonable rates for sales by pipelines to their customers only with respect to amounts paid in a true sale. It did not explicitly repeal the Commission's powers to set such rates for gas produced by a pipeline which is the subject of an intracorporate transaction. This circumstance plainly shows that the "clear and manifest" showing of Congressional intent which is essential to create a repeal by implication is wholly

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[11]Accord: *Perrin v. U.S.*, 444 U.S. 37 (1979); *Burns v. Alcala*, 420 U.S. 575 (1975); *Banks v. Chicago Grain Trimmers Ass'n*, 390 U.S. 459 (1958) *Addison v. Holly Hill Fruit Products*, 322 U.S. 607 (1944).

lacking here. *U.S.* v. *Borden Co.*, 308 U.S. 188, 198 (1939); *Morton* v. *Mancari*, 417 U.S. 535, 550-551 (1974).

The text of Section 601(b)(1)(E) of the NGPA affords additional proof that Congress expressly repealed the Commission's powers under Sections 4 and 5 of the NGA to fix rates only as to production by independent producers and pipeline affiliates. Section 601(b)(1)(A) expressly repeals the Commission's authority to fix rates sold in a "first sale." That section accomplishes this objective by providing that the Commission must accept as the "just and reasonable" rate for purposes of Sections 4 and 5 of the NGA, any price paid which does not exceed the applicable maximum lawful price established under the NGPA.

However, Congress was well aware that even though a pipeline purchases gas in a first sale from its affiliate, there is an absence of arms length bargaining in such transactions. Therefore, Section 601(b)(1)(E)[12] allows the Commission to police such transactions by requiring that " ... in the case of any first sale between any interstate pipeline and any affiliate of such pipeline ... " the price paid shall " ... not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline." There is no similar provision with respect to pipeline production even though the same problem—the absence of arms length bargaining—is present there.

Surely, the absence of a similar safeguard in the case of pipeline produced gas which is the subject of an intracorporate transfer demonstrates that Congress did not intend to include such gas within the statutory concept of a "first sale." It is absurd that a pipeline which produces gas through a separately incorporated affiliate is subject to the comparable price limit of Section 601(b)(1)(E), but that a pipeline which conducts its business as a single corporate entity may charge itself a higher price for its gas than it could legally pay to its production affiliate. Neither the Court below nor any party here has given any logical explanation of the failure of Congress to protect consumers from excessive

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[12]See Add. C. p. A-15 for text of §601(b)(1)(E).

prices in an intracorporate transfer of pipeline production. The only logical inference which can be drawn is that Congress omitted an express provision for such consumer protection because it did not intend that pipeline produced gas which was the subject of an intracorporate transfer be eligible for NGPA maximum ceiling prices. The legislative history of the NGPA confirms the correctness of this conclusion.

The omission of a comparable price test for a pipeline's own production and the inclusion of that test for pipeline production affiliates cannot be attributed to ignorance of the problem. Congressional awareness of the need for equal application of a comparable price test to gas involved in an intracorporate transfer and gas sold by a production affiliate is made manifest by the provisions of Sections 205 and 206 of S.2104, the Senate version of the NGPA. That bill expressly provided for a comparable price test which was applicable to gas produced by an affiliate and by a pipeline from its own properties. Thus, Section 205(B)[13] states in pertinent part:

> Notwithstanding the foregoing, the Commission shall have no power to deny, in whole or in part, any rate or charge made, demanded, or received by any natural-gas company for, or in connection with, the purchase or sale of natural gas, or that portion of the rates and charges of such natural gas company which relates to such purchase or sale, except...
> (B) *in any case where a natural-gas company which transports natural gas in interstate commerce purchases new natural gas from an affiliate or produces new natural gas from its own properties, to the extent that the Commission determines that the rates and charges therefor exceed the current rates and charges, or portion thereof, made, demanded, or received for comparable sales by persons not affiliated with such natural-gas company.* (Emphasis added).

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[13]The language of Section 206(B) of S. 2014, which would have amended Section of NGA is virtually identical to S. 205(B).

The Conference Committee deleted this express provision for the application of the comparable price test to pipeline produced gas. The deletion of such language from a bill which expressly provides for treatment of an issue in a designated manner strongly indicates that Congress did not intend to enact such treatment. *U.S. v. Pfitsch*, 256 U.S. 547, 552 (1921), *U.S. v. Great Northern Railway Co.*, 287 U.S. 144, 155 (1932).

The view that Congress did not provide safeguards against excessive prices in intracorporate transfers because it intended such production to remain under NGA jurisdiction is supported by the legislative history of the 1956 production pricing bill.[14] That bill would have repealed the Commission's power to fix rates for gas produced by both pipelines and independent producers. It expressly differentiated between gas purchased by pipelines from independent producers and gas acquired from affiliates or in intracorporate transfers by establishing a comparable price test for affiliate and pipeline production.[15] The bill was vetoed by President Eisenhower.[16]

Congress in 1956 and in 1978 recognized that deregulation and a free market price do not protect consumer interests where pipeline production affiliates are involved. This strongly militates against the view that Congress intended to make similar non-arms-length intracorporate transactions eligible for higher NGPA price ceilings without any comparable price limitation.

B. The Court Of Appeals Erred In Implying A Repeal Without Any Evidence Of Legislative Intent Or Any Showing That Irreconcilable Differences Exist

The NGPA does not expressly repeal the power of the Commission, under Sections 4 and 5 of the NGPA, to regulate pipeline production. Thus, the Court of Appeals has interpreted the statutory term "first sale" as defined in Section 2(21) in a manner which effectuates an *implied* repeal of the Commission's long established NGA powers to fix "just and reasonable" rates

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[14]H.R. 6645, 84th Cong., 2nd Sess., 1956.

[15]Section 3(F) of H.R. 6645.

[16]Vetoed February 17, 1956.

for such production. This results in a drastic and radical change in the existing relationships between pipelines and their customers as to pipeline gas sold on-system. It retroactively changes the rules of the game so that the consumers who have borne the risks of the development of pipeline reserves will now be deprived of the benefits of their investment.

The Court below concluded that Congress intended such an implied repeal solely on the basis of a *presumed* intent of Congress. The Court admitted there was not a single sentence of legislative history supporting its views, stating:

> [t]he legislative history of section 3301(21) does not illuminate this issue. Congress did not explain its definition of first sale either in the committee reports that accompanied the various drafts of the NGPA or in the discussions that occurred in each House (App. A-10).

It is axiomatic that repeals by implication are not favored, *Posades v. National City Bank*, 296 U.S. 497 (1936). And, if there is no affirmative showing of Congressional intent to repeal, a showing that the earlier and later statutes are irreconcilable is required. *Georgia* v. *Pennsylvania Railway Co.*, 324 U.S. 439, 456-457 (1945); *Morton* v. *Mancari*, 417 U.S. 535, 550 (1974).

In *Columbia Gas Development Corp.* v. *FERC*, 651 F. 2d 1146, (5th Cir. 1981), the petitioner argued that continuation of NGA regulation of a certain category of gas was inconsistent with, and repealed by, the NGPA's incentive pricing policies. The Court held that Congress did not intend "indiscriminate application of the incentive," *Id.* at 160. The Fifth Circuit refused to imply a repeal in that case because there were no irreconcilable differences between the NGA and the NGPA and the two acts could be interpreted in a manner which gave effect to the provisions of both. The Court held:

> Repeal by implication arises when there is a plain repugnancy between the operation of two acts or their

> provisions, but repeals by implication are not favored, and the two acts or provisions thereof are to be given effect consistent with each other whenever possible. *See United States* v. *Tynen,* 11 Wall. 88, 78 U.S. 88, 92, 20 L.Ed. 153 (1870). When interpreting and construing two acts that affect one particular subject matter or area, the court must attempt to reconcile the acts, if possible, so as to produce a symmetrical whole. *(Id.,* 1158).

In the instant case, however, the same Court did not explain why NGA pricing of pipeline production is inconsistent with the NGPA, did not attempt to show that irreconcilable differences exist between the two Acts, and did not attempt to reconcile the Acts. Without such findings, the Court had no right to find an implied repeal of the Commission's NGA powers to price natural gas produced by pipelines.

C. Past Congressional Action In Expressly Repealing The Commission's Powers Over Pipeline Production Makes It Most Unlikely That Congress Repealed The NGA By Implication In The NGPA.

Past Congressional actions in bills affecting Commission powers over gas producers shows that Congress has never elected an implied repeal. Thus, in 1950 and 1956, Congress passed bills which would have deregulated the production of natural gas. In 1950, Congress passed H.R. 1758, 81st Cong., 2d Sess., which would have deregulated the production of natural gas at the wellhead. That bill, which was vetoed by President Truman, specifically excluded production by pipelines and pipeline affiliates from its provisions. Section 2 of that bill amended Section 1 of the NGA by adding a new Subsection (c), which stated:

> The provisions of this Act shall not apply (1) to any arm's length sale of natural gas by a producer or gatherer, at or prior to the point of delivery thereof into interstate transmission facilities of a natural-gas company, or (2) to incidental transportation thereof, by the producer or gatherer, necessary for its delivery pursuant to or in

consummation of any such sale: Provided, however, that this subsection shall not apply if the producer or gatherer is otherwise engaged in, or controls, is controlled by, or is under common control with, another person who is otherwise engaged in, the transportation of natural gas in interstate commerce or the sale in interstate commerce of natural gas for resale for ultimate public consumption.

In 1956, Congress passed H.R. 6645, 84th Cong., 2d Sess. That bill, which was vetoed by President Eisenhower, would have deregulated *all* production including pipeline production. This bill recognized the differences between independent production and pipeline (including affiliate) production, but treated them substantially alike. However, Congress once again used express language to show its intent with respect to pipeline and affiliate production. These provisions of Section 2 of the bill, which were amendments to Section 5 of the NGA, provided:

"(b) When an increase in any rate or charge for natural gas is filed with the Commission by a natural-gas company and is based in whole or in part upon any contract, executed or renegotiated after the date this subsection takes effect, *for the purchase of natural gas from a person other than an affiliate,* the Commission shall determine, unles there has been a prior determination under subsection (c) of this section, whether the price at which the natural-gas company has contracted to buy such natural gas is the reasonable market price thereof at the point at which the gas is delivered into the transportation facilities of the natural-gas company in or within the vicinity of the field or fields where produced. After such determination, the natural-gas company shall be allowed to charge as an operating expense for natural gas purchased under the contract only such part of the contract price as does not exceed such reasonable market price. In determining the reasonable market price of natural gas under the provisions of this section 5, the Commission shall consider, among other things, *whether such price has been competitively arrived at ... .*

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"(f) In regulating the rates and charges of a natural-gas company, the Commission shall allow as an operating expense of such natural-gas company, *for natural gas produced by it,* the reasonable market price of such natural gas at the point at which the gas is delivered into the transportation facilities of the natural-gas company in or within the vicinity of the field or fields where produced, and *for gas purchased from an affiliate,* the amount paid to such affiliate for such gas up to but not in excess of the reasonable market price of such natural gas at the point at which the gas is delivered into the transportation facilities of the natural gas company in or within the vicinity of the field or fields where produced. (Emphasis added).

Moreover, the House Report on H.R. 6645, H.R. Rep. 84-992, 84th Cong., 1st Sess., dealt at length with the congressional intent to deregulate pipeline and affiliate production. At pp. 11-12 of that Report,[17] the Committee stated:

> The new subsection (f) grants the same treatment to pipeline producers as to independent producers, namely, the allowance of a reasonable market price for the gas, and thereby will encourage the pipelines to expand their production and exploration activities. The net results of this policy will be better service at lower cost to the consuming public.

Here again, Congress thought the question of whether pipeline and affiliate production should be treated the same as independent production was worth a specific and express statement of intent. Thus, whenever the subject of natural gas pricing decontrol has arisen in the past, the Congress has recognized the unique character of pipeline and affiliate

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[17]The full text of the pertinent portions of that Report (pp. 9-12) is set out in Addendum A to this Brief.

production and addressed it specifically. It did so again in the NGPA as to affiliate production. Its failure to do so as to intracorporate transactions is a strong indication that it intended to leave the regulation of such pipeline production as it found it — *i.e.*, the bulk of it subject to NGA cost of service regulation. Consequently, the principle that powers granted by a prior act are presumed to be intact unless specifically or necessarily repealed by a later act is applicable here. *U.S.* v. *Greathouse*, 166 U.S. 606 (1897).

D. The Court Below Ignored The Pertinent Legislative History Of The NGPA Which Shows That Congress Did Not Intend To Deregulate Pipeline Production.

The legislative history of the NGPA also provides a strong indication that no repeal of NGA jurisdiction over pipeline production was intended. The House version of the NGPA was H.R. 8444, 95th Cong., 1st Sess. Sections 405, 406, and 407, governing old natural gas, applied only to "*first sales*" under "*contract.*" As the Commission pointed out in Order 102, pipeline production is the subject of neither a sale nor a contract (App. B-65-66). In addition, Sections 404 and 409 which governed new gas and high cost gas, respectively, applied only to first sales. H.R. 8444 contained no definition of first sale,[18] but whether the common meaning or the NGA meaning of sale (App. B-65) is applied, *no* pipeline production could have been included.

In addition, Sections 416 and 417(a) and (b) of H.R. 8444 which specifically amended Sections 1(b), 4 and 5 of the NGA,

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[18]The House Report, House Report No. 95-53, Vol. II, 95th Cong. 1st Sess., does address the definition of "first sale." In a section entitled "Maximum Lawful Price-First Sale Concepts," *Id.* p. 399, the Committee stated:

> *The Committee intends that the term "first sale" be applied by the Federal Power Commission to the first transfer of natural gas for value. Therefore, the first sale price is essentially a wellhead price.* (Emphasis added).

contain no comparable pricing provision similar to that in Section 601(b) (E) of the NGPA. It is unlikely that the House would have voted to deregulate pipeline production without such a safeguard.

The Senate version of the NGPA—S. 2104—took an entirely different tack. Section 24(b) totally deregulated new gas which was defined in Section 204(7) as gas from a well developed after January 1, 1977, from either a new reservoir or an extension of an existing reservoir, but it left "old" natural gas subject to NGA regulation (See § 203 of S. 2104 which added a new paragraph (2) to subsection 1(b) of the NGA). Since most pipeline cost of service production would be old gas under this definition, such pipeline production would not have been deregulated.

In addition, as noted above (*supra, p. 19)* Sections 205 and 206 of S. 2104 amended Sections 4 and 5 of the NGP by specifically deregulating new pipeline and affiliate production subject only to a comparable price test.

The inescapable conclusion is that the House intended to preserve NGA regulation of all pipeline production and the Senate intended to preserve it with respect to "old" gas. Therefore, both Houses provided that regulation of "old" pipeline production under the NGA should continue.

Logic alone dictates that the final version of the NGPA would not provide for more than either the House or Senate bill. But, House Rule XXVIII. 3, which defines the jurisdiction of conference committees in terms of the germaneness of amendments proposed in conference between the Houses, makes it clear that the Conference Committee is not permitted to expand the final version beyond the bills submitted by the two Houses. Thus, the comments on House Rule XXVIII. 3, p. 642, state:

> While the scope of differences committed to conference—where one House has amended an existing law and the other House has implicitly taken the position of existing law by remaining silent on the subject—may properly be measured between those issues presented in the amending language and comparable provisions of existing law, the inclusion in

> a conference report of new matter not specifically contained in the amending version and not demonstratably contained in existing law may be ruled out as an additional issue not committed to conference in violation of this clause.

Similarly, Section 546 of Jefferson's Manual provides:

> The managers of a conference must confine themselves to the differences committed to them...and may not include subjects not within the disagreements...even though germane to a question in issue. (Citations omitted).

Since the two Houses agreed that old pipeline production would continue under NGA regulation, the Conference Committee could have either continued NGA control over all such production or deregulated new pipeline production. It lacked authority to deregulate all pipeline production. In holding that the Conference Committee terminated NGA regulation over all pipeline production, the Court below in effect held that the Committee exceeded its powers. This is clearly an erroneous conclusion. For, it is well settled that:

> A Conference Committee lacks power to make substantive changes on matters about which both Houses agree.

Union Electric Co. v. *EPA*, 427 U.S. 246 (1976), citing *National Coal Operators Ass'n v. Kleppe*, 423 U.S. 388, 401, n. 10 (1976), at 262-263.

E. The Judicial Repeal By Implication Made By The Court Below Produces Inequitable Results

Finally, a repeal of the Commission's powers under the NGA to establish rates on a cost related basis for pipeline production would retroactively change ratemaking policy to the significant detriment of the consuming public. This is because, in the case of pipeline cost of service properties, the entire risk of loss attributable to exploration and development of reserves was fully paid by consumers. Under cost of service pricing a pipeline wishing to engage in exploration purchased a lease. The cost of the lease was included in its rate base. Once the pipeline began exploration, the cost of exploration was included in rate base if the pipeline was successful. If the exploration effort failed,

the expenses were included in the cost of service and paid by the consumers.

Therefore, the entire risk of failure by a pipeline engaged in exploration was borne by the pipeline's customers, and the pipeline was reimbursed for 100% of its exploration expenses—whether its exploration efforts were successful or not. In addition, if the pipeline did discover gas, the total cost was included in rate base and the pipeline earned a return on this expense. Moreover, since the pipeline had a captive market for its gas, it was never concerned that its gas might be unmarketable due to price, location or quality.

The customer's *quid pro quo* for its investment was that when the pipeline was successful, it obtained a secure supply of gas at a reasonable and stable price.

For these reasons, the Commission pointed out in Order 98 (App. B-26 to B-27) that:

> [p]ipelines receiving such treatment have enjoyed the advantage of passing on to their customers the risks of the pipeline's production ventures. Pipelines have passed on the cost of acquiring leases and the costs of exploration and development, including dry hole costs and other costs associated with unsuccessful and marginally successful ventures, in exchange for assuring their customers the opportunity to enjoy the additional volumes resulting from successful ventures at a price determined on a cost-of-service basis. The Commission therefore will not extend pricing parity to pipeline production which prior to the enactment of the NGPA was valued on a cost-of-service basis rather than by reference to area or nationwide [rates].

In Order 102, the Commission again found that "a pipeline whose production is valued on a cost-of-service basis will receive a rate that, over time, provides for the recovery of all prudently incurred costs plus a reasonable return on investment" (App. B-73). The Commission concluded that to "vary this policy ...would deprive [pipeline customers] of price benefits they

should receive in exchange for assuming the risk of a pipeline's production ventures" *(Ibid.)*[19]

There is a well established principle of utility ratemaking that the party which has assumed the risk of loss in a venture is entitled to any gains therefrom. In *Democratic Central Committee* v. *WMATC*, 485 F.2d 786, 806 (D.C. Cir. 1973), the Court held:

> We think two accepted principles which have served comparably to effect satisfactory adjustments in other aspects of ratemaking can do equal service here.
>
> One is the principle that the right to capital gains on utility assets is tied to the risk of capital losses. *The other is the principle that he who bears the financial burden of particular utility activity should also reap the benefit resulting therefrom.* (Emphasis added).

The ratemaking changes mandated by the Court below are inequitable not only because the consumer would now be deprived of the benefits of his bargain with the pipeline, but because this clearly applicable principle would be repudiated. No intent to deal so cavalierly with the rights of consumers and with established regulatory principles should be ascribed to Congress in the absence of a specific recitation of such intent.

II. THE COURT BELOW ERRED IN HOLDING THAT AN INTRACORPORATE TRANSFER IS A "SALE" UNDER THE NGPA

The Commission held that an intracorporate transfer of gas from a pipeline to itself was not a "sale" as that term had been defined in the agency's adminstration of the NGA (App. B-65-66).[20] The Court rejected this view and based its entire decision on

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[19]A change from cost of service ratemaking to NGPA prices for that gas for which the consumer contributed the capital for exploration and development would quite simply unjustly enrich the pipeline's stockholders, who bore no risk, but who would be the sole beneficiaries of higher prices paid for this gas.

[20]While holding that an intracorporate transfer is not a "first sale" under Section 2(21) (App. B-2-3), the Commission overlooked the vital point that under the definition of sale in §2(20) of the NGPA, such a transfer could be neither a sale nor a first sale. Thus, both the Court and the Commission completely overlooked this controlling section. This issue is dispositive and makes it unnecessary for this Court to determine

the proposition that the "...NGPA contemplates that the pipeline is both a buyer and seller as to its own production" (App. A-8). On the basis of this "novel regulatory doctrine,"[21] the Court below held that the NGPA requires the Commission to impute a fictitious "first sale" to the intracorporate transfer of gas from one division of a pipeline to another at the wellhead (App. A-11-12).

Unless there is a "sale," there cannot be a "first sale." This conclusion follows from the statutory text and from the fact that these two terms are both defined in Section 2 of the NGPA. These definitions are obviously in *pari materia*, and so the narrower term must be construed in light of the broader, *Neal v. Scruggs*, 95 U.S. 704, 708 (1878).

Plainly then, an NGPA "first sale" cannot include any transaction which is not a "sale" under that statute. We shall prove that an intracorporate transfer is not a "sale" from the NGPA definition of that term.

Section 2(20) provides:

> (20) SALE.— the term "*sale*" means any *sale, exchange*, or other *transfer for value*. (Emphasis added).

The NGPA does not define specifically the meaning of any of the underlying terms in the definition of sale. However, the Conference Committee stated "[t]he definitions provided in the Act are generally self-explanatory, except as noted." S.Rep. 95-1126, 95th Cong., 2d Sess., p. 69.

Clearly, a definition is only self-explanatory if the ordinary meaning of the words used therein applies. Since there is no explanation of the definition of sale in the legislative history, it is clear that Congress intended the ordinary meaning of the words "sale," "exchange," and "transfer for value" to apply.

Black's Law Dictionary (5th Ed.) defines these terms as:

> SALE. A contract between two parties, called, respectively, the "seller" (or vendor) and the "buyer," (or purchaser) by

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[21]Solicitor General's Petition for Certiorari, p. 11.

> which the former, in consideration of the payment or promise of payment of a certain price in money, transfers to the latter the title and the possession of property. (P. 1503; citations omitted).
>
> EXCHANGE. To barter; to swap...To part with, give or transfer for an equivalent... (p. 671; citations omitted).
>
> TRANSFER. An act of the parties, or of the law, by which the title to property is conveyed from one person to another. (p. 1669; citations omitted).

An intracorporate transfer cannot satisfy the ordinary meaning of the term "sale," "exchange," or "transfer for value" because the single pipeline corporation involved is only one entity, and each of these transactions in its ordinary meaning, requires two separate parties. Specifically, there must be a separate buyer and seller in order to have a sale.

This conclusion is reinforced as to pipeline production by Section 2(22) of the NGPA which defines the term "delivery" in the context of a first sale as meaning "....the physical delivery *from the seller....*" (Emphasis added.)[22] There is, of course neither seller nor buyer in an intracorporate transaction.

Furthermore, the second element of a conventional "sale" or exchange is that there be a reciprocal transfer of elements having value. Here, no consideration is paid or commodity exchanged when the production division of a pipeline or transfers gas to another division of the same pipeline. The intracorporate transaction clearly is not a transfer, which is defined as the passing of property from one person to another. Furthermore, the second element of a conventional "transfer for value" is also absent since the term "value" is synonymous with "consideration." *Black's Law Dictionary* (5th Ed., p. 1391).

Therefore, the intracorporate transfer simply does not qualify as a "sale" under the literal language of the NGPA.

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[22]See Addendum Co, p. A-13, for the text of §2(22).

Moreover, a general rule of statutory construction requires that language in a federal statute be given its ordinary meaning. This principle has been specifically applied to a statute which used the terms "sale" and "exchange." *Commissioner of Internal Revenue v. Brown,* 380 U.S. 563, 571 (1965).

Thus, the Court below disregarded the express directive by Congress that the definitions used in the NGPA are self-explanatory, as well as the general rule of statutory construction that language be given its ordinary meaning. Surely, if Congress had intended to treat a pipeline as both a buyer and seller of its own production, it would have expressly so provided.

Last, but not least, the Court below violated the cardinal principle of statutory construction which is that the rules of statutory construction are only applicable in ascertaining the meaning or application of words otherwise obscure or doubtful. *Russell Motor Car Co.* v. *United States,* 261 U.S. 514, 519 (1923). Inferences as to Congressional intent cannot be used to alter the plain meaning of the language. Here, the plain language of the NGPA speaks for itself and makes irrelevant the tortured construction of that statute by the Court below.

The NGPA definition of a statutory "sale" in a manner which excludes intracorporate transfers is not a mere technicality but reflects the real and important substantive differences between intracorporate transfers and normal sales in the gas pipeline industry. These differences were noted by the Commission and advanced as its reason for refusing to treat intracorporate transfers as sales. Thus, the Commission stated (App. B-65-66):

> In its administration of the NGA, the Commission has not treated as a sale the transfer of pipeline produced gas into the transmission system of that pipeline. *No contracts govern that transfer; no certificates under the NGA have been issued or were required for that transfer.* The proper implementation of the NGPA, which only minimally disturbs the Commission's rules of law that govern pipeline ratemaking under the NGA, does not as a practical matter compel us to vary that policy.
>
> To the contrary, we believe that such an interpretation of the term sale would prove difficult to reconcile

> administratively with certain provisions of the NGPA. For example, the maximum lawful price under Section 104 assumes the existence of a just and reasonable rate applicable to the sale of natural gas prior to the enactment of the NGPA. However, because the pipeline's intracorporate transfer was not a sale under the NGA, there was no just and reasonable rate applicable to that transfer. Also, the provisions of Section 315, governing the duration of contracts, bona fide offers, and right of first refusal depend upon the existence of a contract for their applicability and effect. *These provisions, which provide purchasers of gas from independent producers with some assurances of continued supply, are inapplicable to a pipeline that "sells" natural gas in a first sale to itself.* (Emphasis added).

For these reasons, the Court below plainly erred in ignoring the express language of Section 2(20), inventing an unprecedented, fictitious "imputed" wellhead sale as to such intracorporate transfers and disregarding the express intent of Congress concerning the standards to be applied in interpreting the definitions in Section 2 of the NGPA.

III. THE COURT BELOW INTERPRETED SECTION 2(21), THE STATUTORY DEFINITION OF A "FIRST SALE," IN A MANNER WHICH DEPRIVES IT OF ALL MEANING.

The Commission found that intracorporate transfers of pipeline production did not constitute "first sales". The Commission based this conclusion on the fact that the captions in Title I[23] and the legislative history[24] of the NGPA make it clear

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[23]The caption of Title I is "WELLHEAD PRICING." The caption of Subtitle A of Title I is "WELLHEAD PRICE CONTROLS."

[24]H.R. Rep. 95-543, 95th Cong. 1st Sess. Vol. II, p. 399, states:

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> The Committee intends that the term "first sales" be applied by the Federal Power Commission to the first transfer of natural gas for value. Therefore, the first sale price is essentially a wellhead price.

that Congress intended to afford higher incentive prices to producers of gas making sales at the wellhead. Therefore, the Commission was compelled to find that a pipeline which produced gas, used it as part of system supply and transported it from the point of production to the *point of sale had not made a wellhead sale.* The Commission rejected the request by certain pipelines that it "impute" a sale at the wellhead by the pipeline to itself on the ground that such a fiction was contrary to reality (App. B-65-66).

While the Court below did not disagree that no wellhead sale occurred, or that such a sale was essential to qualify for NGPA prices, it did disagree with the Commission on the imputed sale. First, it stated the sound proposition "that Congress intended the sale by the producer of the gas to be the first sale" (App. A-11). Second, it concluded that " ... this would mean that the intracorporate transfer from the production division of the pipeline to the transportation division of the pipeline would constitute the first sale" *(Id.).* The Court did not cite any portion of the NGPA or its legislative history which supported this view. Thus, the decision below can only be sustained if the NGPA definition of a "first sale" includes a fictitious "sale" at the wellnead between a pipeline and itself and is so clear that it overrides the contrary interpretation by the Commission.

But, the plain language of Sections 2(21)(A) and (B) makes it clear that intracorporate transfers of pipeline produced gas do not qualify for NGPA maximum ceiling prices. Section 2(21) (A) sets forth a "General Rule" defining "first sale". Then, Section 2(21)(B), captioned "Certain Sales Not Included," expressly excludes from the statutory category " ... the sale of any volume of natural gas *by* any interstate pipeline ... unless *such sale* is attributable to volumes of natural gas produced by such interstate pipeline ..." (Emphasis added). Only the *exceptional* pipeline sale can be a "first sale." A pipeline sale can qualify for NGPA prices only when *"such sale is attributable"* to gas produced by that pipeline. Section 2(21)(B) unequivocally requires that *all* of the sale, not *part* of it, be attributable to pipeline produced gas. The Court below rewrote this language to fit its fictitious wellhead sale theory.

The Commission properly noted that Congress did not say a portion of the sale or a *pro rata* share of the sale had to be attributable to volumes produced by the pipeline (App. B-4). It rejected requests by pipelines that in situations where the pipeline had purchased a portion of its gas supply from independent producers and produced the remainder, the "sale" should be attributed to the *pro rata* portion of the gas produced by the pipeline. *Without expressing any disagreement with this interpretation of the statute, the Court below reached exactly the result desired by the pipelines. It did so by imputing a fictitious sale by the pipeline to itself at the wellhead.* The practical result of such imputation is to afford NGPA prices to the *pro rata* share of a pipeline's overall gas supply comprised of its own production.

The Court below also erroneously concluded that the Commission's reading of the "unless" clause of Section 2(21)(B) would render that clause a nullity (App. A-8). The Court ignored Order No. 58 which permitted NGPA pricing "if a pipeline were to sell its production at the wellhead in an off-system sale" (App. B-2) and if the pipeline were to "dedicate natural gas which it produced from an identifiable source to a purchaser by contract, commingle the gas with general supply gas and withdraw equivalent volumes for delivery to that purchaser" *(Id.* at B-3). In the latter instance, the Commission permitted NGPA pricing of *on-system* sales so long as there is an identification of the gas *by contract.* The Court erroneously concluded that the "unless" clause would only have meaning if interpreted as granting "first sale" status to gas at the wellhead under an imputed fictitious sale (App. A-8-9).

On the contrary, the Commission's interpretation gives life to the "unless" clause and reflects its long-settled policy. The Commission has always granted the same treatment to off-system sales by pipelines as it has afforded to independent producers. Prior to the NGPA, and acting under the NGA, the Commission reaffirmed this long standing policy in the *Pipeline Production Area Rate Proceeding,* 42 FPC 738 (1969) *aff'd sub nom. City of Chicago v. FPC,* 458 F.2d 731 (D.C. Cir. 1971), *cert. den.,* 405 U.S. 1074 (1972). There, the Commission stated that it was:

> [n]ot primarily concerned in this proceeding with pipeline production sold off system to other pipelines. We think that the applicable area rate should apply to such production. (at 746).

Parity of pricing for off-system sales was permitted even though the Commission continued its historic policy of cost of service pricing for on-system sales of most pipeline produced gas. Thus, long before the NGPA was enacted, off-system *wellhead* sales were given area or national rates, while on-system *downstream* sales were generally given cost of service rates. Section 2(21) of the NGA merely codified existing agency practice and law.

In addition, Congress must certainly have contemplated that the "unless" clause would be the exceptional situation rather than the usual situation or it would not have placed the clause in a subordinate position and in a conditional tense.

In the process of correcting an error the Commission had not made, the Court below committed a blatant and egregious error. It effectively eviscerated and nullified the *entire* first sale clause by depriving it of any meaning. There is no dispute that independent producers making wellhead sales are engaged in "first sales." Likewise, pipeline production affiliates engaged in wellhead sales are also making such sales. If every intracorporate transfer of pipeline produced gas is *also* a "first sale," then the same must be true of intrastate pipelines and local distribution companies and industrial concerns which are also producers. This means that under the interpretation of "first sale" by the Court below, every transfer of gas produced in the United States is a statutory first sale. If this is the case, there was clearly no need for Congress to limit the applicability of the NGPA to those transactions which qualified as statutory first sales.

IV. THE COURT BELOW ERRED WHEN IT USED PERIPHERAL HISTORY OF THE NGPA TO SUPPORT ITS VIEW

A. The Legislative History Does Not Support The View That An Intracorporate Transfer Is A First Sale.

The Court below relied heavily on a particular portion of the Conference Report, S.Rep. No. 95-1752, 95th Cong., 2d Sess., p. 116, to support its position. The Court stated (App. A-12):

> Support for the proposition that the intracorporate transfer constitutes a first sale is contained in the conference committee report. In discussing the Commission's power to define terms in the NGPA, the Committee stated:
>
> > the Commission may define terms such as "transfer for value" used in the definition of first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition.

The Court reasoned that:

> This comment assumes that intracorporate transactions will fall within the first sale definition. The decision which Congress committed to the Commission's judgment was whether regulations were necessary to govern those transactions. The fact that the Commission was permitted to regulate intracorporate transactions under the first sale definition does not imply that Congress did not intend in the first instance for them to be treated as first sales. (App. A-12-13).

There are several flaws in the Court's reasoning. First, the Committee incorrectly stated the facts from which it drew its conclusions. The term "transfer for value" is not "used" in the definition of first sale. Rather, the term "transfer for value" is used in § 2(20) which defines the term "sale." Thus, the Conference Report is in error and is entitled to no weight.

In addition, this is a classic example of the unfortunate practice of using language in Committee Reports in a manner which contradicts the plain language of the statute. In *National Small Shipments* v. *CAB*, 618 F.2d 819 (D.C. Cir. 1980), the District of Columbia Circuit criticized this practice and rejected the use of such misleading legislative history. The Court held (at 828):

> Thus the literal language of the statute should control the disposition of this case. The Air Carriers would have us construe the statute in a manner that is inconsistent with its plain language. But as this Court has previously noted, "We find no mandate in logic or in case law for reliance on legislative history to reach a result *contrary* to the plain meaning of a statute, particularly where that plain meaning is in no way unreasonable." *United Air Lines, Inc.* v. *CAB, supra,* 569 F.2d at 647 (Emphasis in original).

> Courts in the past have been able to rely on legislative history for important insights into congressional intent. Without implying that this is no longer the case, *we note that interest groups who fail to persuade a majority of the Congress to accept particular statutory language often are able to have inserted in the legislative history of the statute statements favorable to their position, in the hope that they can persuade a court to construe the statutory language in light of these statements. This development underscores the importance of following unambiguous statutory language absent clear contrary evidence of legislative intent.*
>
> Our conclusion that the plain language of the statute should control is buttressed by the Air Carriers' inability to point to any "*clear contrary evidence* of legislative intent." *Nat'l Railroad Passenger Corp. v. Nat'l Ass'n of Railroad Passengers,* 414 U.S. 453, 458, 94 S.Ct. 690, 693, 38 L.Ed 2d 646 (1974) (First and third emphasis in original).

Since the plain language of this statute comports with the Commission's interpretation and there is no "clear contrary evidence of legislative intent," the *Mid-Louisiana* Court's interpretation must fall.

Second, the quoted portion of the Conference Report states that the Commission *"may"* establish rules applicable to intracorporate transfers under the first sale definition. This language is, *at most,* permissive and does not require the Commission to promulgate any rule. Consequently, the Court could not interpret this Conference Report to require the promulgation of the specific rule which the Commission expressly refused to adopt (App. B-65-66).

B. The Court Below Applied The Wrong Standard For Judicial Review

Section 501(a) of the NGPA directed the *Commission* to administer the NGPA. Section 501(b) authorized the *Commission* to promulgate rules defining terms used in the NGPA. Section 501(b) provides:

> AUTHORITY TO DEFINE TERMS.—Except where otherwise expressly provided, the Commission is

> authorized to define, by rule, accounting, technical, and trade terms used in this Act. Any such definition shall be consistent with the definitions set forth in this Act.

The only limit placed on the Commission's authority is that the regulations it promulgates must be consistent with the definitions set forth in the NGPA.[25] The Court's "first sale" interpretation plainly conflicts with the statutory definitions of *both* a "sale" and a "first sale." Therefore, it must be reversed.

The Court below approached the problem of the validity of Order 58 as if it involved only a pure question of law, i.e. the interpretation of statutory language. On the basis, the Court erroneously concluded, contrary to precedent,[26] that it did not need to defer to the agency's interpretation of its own enabling Act. But, on its face, Order 58 promulgated a codified *substantive rule*. Furthermore, as the Commission expressly held, the choice of the meaning to be given by that rule to the NGPA concept of a "first sale" had important administrative and policy consequences[27] which only the agency had the necessary expertise and legal authority to consider and determine. Plainly, the Court applied the wrong standard for judicial review of a mixed question of policy and law to an agency which—whether it was making a substantive rule or defining, by rule, terms used in the NGPA—had express authority to take such action.

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[25]Thus, we deny the Commission's claim that it has authority to adopt a rule treating an intracorporate transfer as a "first sale." (App. B-65).

[26]*Fed. Elec. Com'm* v. *Dem. Senatorial Campaign Com.*, 102 S.Ct. 38, 45 (1981).

[27]It found, *inter alia*, that if pipeline or distributor production were the subject of a fist sale at the actual point of sale: (1) it would be forced to regulate retail sales, which would effectively extend its authority beyond the wholesale level (App. B-4); (2) pipelines and distributors with and without production properties would be regulated differently *(Id.)*; and (3) regulation of pipeline wholesale sales would be carried out under two statutes in proportion to the amount of such production of each pipeline (App. B-5).

V. THE COURT BELOW UNLAWFULLY USURPED THE ADMINISTRATIVE FUNCTIONS OF THE COMMISSION IN VACATING ORDER 98.

The Court below held that since the Commission lacked authority to set prices for interstate pipeline production under the NGA, those prices would have to be set under the NGPA (App. A-15). On this basis, the Court vacated Order No. 98 without considering its merits merely because Order No. 58 was void, stating (App. A-15):

> Because we hold that the Commission lacked authority to set prices for interstate pipeline production under the NGA, we also vacate Order No. 98 without reaching the issues of arbitrary pricing raised here.[4]

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[4]...The effect of our holding with respect to Order No. 58 is that the price for pipeline production will now be set under the NGPA....

This action raises the question of whether the NGPA has impliedly repealed Commission jurisdiction under Section 1 (b), 4 and 5 of the NGA over *all aspects* of the pricing of natural gas.

Order 98 did not set any price or rate for natural gas. Rather, it barred those pipelines which had received cost of service, whether through general rules, or by a rate settlement or a "special exception" granted by Commission order, from collecting higher NGPA rates. The Commission promulgated Order 98 on the basis of its legal conclusion that intracorporate transfers of pipeline produced gas were not "first sales" under the NGPA, and therefore, would continue to be regulated under the NGA. Neither the Commission nor the Court addressed the question of whether any agency jurisdiction under the NGA would have survived if intracorporate transfers of pipeline production were NGPA first sales (App. B-71). Had the Commission known the question was at issue, it could have written this same order in terms of its NGA powers over *pipeline rate filings.*

The Court below found that the Commission had committed legal error in concluding that it still had NGA powers over the pricing of intracorporate pipeline production. But, whether or

not the Court was correct in voiding Order 58, it clearly exceeded its powers when it vacated Order 98 instead of remanding that rule to the Commission for further consideration. When an administrative agency has adopted an agency rule or order on the basis of a mistaken interpretation of its legal powers, the reviewing court has only the power to uncover an error of law and it must remand the case to the agency. *FPC* v. *Idaho Power Co.*, 344 U.S. 17, 20 (1952); *FCC* v. *Pottsville Broadcasting Co.*, 309 U.S. 134 (1940).

The determination of whether or not any NGA pricing or other authority survives which will legally support part, or all, of the regulations promulgated by Order 98 is an administrative function exclusively within the jurisdiction of the Commission. *Securities and Exchange Commission* v. *Chenery Corp.*, 318 U.S. 80, 88-89 (1942). Since this is the case, this determination must be made by the regulatory agency in the first instance.

For these reasons, this Court must reverse the action of the Court below in vacating Order 98, even if it affirms the reversal and vacation of Order 58.

In addition, it is patently clear that the NGPA does not repeal or nullify the rate filing requirements of NGA Section 4 as to either pipelines or independent producers. As the Fifth Circuit held in *Columbia Gas, supra,* at 1155-59, mere eligibility by an independent producer for higher NGPA maximum ceiling prices does not automatically entitle that producer to collect such prices, because the NGPA did not repeal or nullify the rate filing requirements of NGA. The Court below plainly erred in assuming that if a pipeline producer was engaged in making a first sale, it was automatically entitled to NGPA prices and relieved of the necessity to make a Section 4 rate filing. The NGPA cannot give pipeline producers more than equality with independent producers. Therefore, the fact that this rate filing jurisdiction on the part of the Commission has not been repealed inevitably means that it has the right to consider, on remand, whether it should recast Order 98 in terms which will survive whatever loss of direct pricing power it may have suffered under the NGPA.

CONCLUSION

WHEREFORE, for the foregoing reasons, AEPCO respectfully requests that this Court reverse and set aside the judgment and decision of the Court below and direct that Court, on remand, to affirm Order 58 and consider the lawfulness of Order 98 on its merits.

If this Court should affirm the judgment of the Court below with respect to Order 58, AEPCO further requests that it nevertheless reverse and set aside the judgment of the Court below as to Order 98, and remand that cause to the Court below with directions to remand that Order to the Federal Energy Regulatory Commission for further consideration.

Respectfully submitted,

ARIZONA ELECTRIC POWER
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November 29, 1982

ADDENDUM A

HOUSE OF REPRESENTATIVES

84TH CONGRESS
1st Session

REPORT
No. 992

TO AMEND THE NATURAL GAS ACT, AS AMENDED

* * * *

[Page 9]

Pipeline-Produced Gas Treated In Same Manner As Purchased Gas

Under the new subsection(f) which would be added to section 5 of the act by section 3 of the bill, the Commission, for rate purposes, would treat gas produced by a natural-gas pipeline company or pur-

[Page 10]

chased by it from an affiliate, on the same basis as it treats gas purchased in an arm's-length transaction from a nonaffiliate.

It is provided that for gas which it produces itself it will be allowed, as an operating expense, the reasonable market price of the gas, and for gas which it buys from an affiliate it shall be allowed, as an operating expense, the amount paid to such affiliate up to but not in excess of the reasonable market price.

In the process of ratemaking, the Commission, prior to its decision of April 1954, in the matter of the Panhandle Eastern Pipe Line Co., had treated all producing facilities which were owned by a pipeline company in the same manner as its transportation facilities, namely, as part of the net investment rate base—the company being allowed to earn a reasonable return on such rate base. That treatment resulted in discrimination between the treatment of gas produced by the pipeline, or purchased from an affiliate, as against the treatment accorded gas purchased by the pipeline.

The Commission's earlier procedures yielded incongruous results in the field which are well described by Mr. Justice

Jackson in *Colorado Interstate Gas Co.* v. *Federal Power Commission* (324 U.S. 581, 610, 611):

To let rate-base figures compiled on any of the conventional theories of ratemaking govern a rate for natural gas seems to me little better than to draw figures out of a hat. These cases confirm and strengthen me in the view I stated in the Hope case that the entire rate-base method should be rejected in pricing natural gas, though it might be used to determine transportation costs. These cases vividly demonstrate the delirious results produced by the rate-base method. These orders in some instances result in three different prices for gas from the same well. The regulated company is a part owner, an unregulated company is a part owner, and the landowner has a royalty share of the production from certain wells. The regulated company buys all of the gas for its interstate business. It is allowed to pay as operating expenses an unregulated contract price for its coowner's share and a different unregulated contract price for the royalty owner's share but for its own share it is allowed substantially less than either. Any method of ratemaking by which *an identical product from a single well, going to the same consumers, has three prices* depending on who owns it does not make sense to me.

These cases furnish another example of the capricious results of the rate-base method in this kind of case. The Commission has put 5 of the most important leaseholds, containing approximately 47,000 acres, in the rate base at $4,244.24, something under 10 cents per acre. Three such leases are put in the rate base at zero. This is because original cost was used, and these were bought before discovery of gas thereon. The company which took the high risk of wildcat exploration is thus allowed a return of 6½ percent on nothing for the 3 leases and a return of less than $300 a year on the others. Their present market value is shown by testimony to be over $3 million.

I cannot fairly say that the Commission exceeded its jurisdiction in obtaining this evidence and making these calculations even though the evidence related to production and gathering of gas. But I do think it is a fantastic method of fixing a "just and reasonable" price for gas. [Italics supplied.]

As a consequence of the Commission's past practices, the amount of gas produced by the natural-gas pipeline companies declined proportionately to that which they purchased. In 1940, 8 major pipelines produced more than 47 percent of the gas they

transported and sold, whereas in 1952 only 18½ percent of total requirements were produced by 15 major systems then operating in interstate commerce. Many pipelines disposed of their gas properties, and others did not undertake to enter into the ownership or operation of gas-producing properties and facilities.

[Page 11]

In proposing that natural gas produced by a natural-gas company or one of its affiliates be treated as a commodity, in contradistinction to its being considered as part of the net investment rate base and accorded the utility rate-base approach, the committee action is in conformity with the opinion advanced during the hearings by Commission Chairman Kuykendall:

> We believe that the proposed legislation*** would result in equal treatment of producers, would encourage the ownership and operation by pipeline companies of their own producing and gathering properties, and would definitely and conclusively contribute to the soundness and the security of the sources of gas supply, and the maintenance of adequate service. Those results would, inevitably, redound to the benefit of the domestic, as well as other customers, and, it is our belief, would achieve in the long run lower rates for natural gas. While we are interested in reasonable rates, we must be equally concerned with the financial stability of the utilities under our jurisdiction, the safety of the investments which have been made in them, and, of equal or greater importance, the continued maintenance of adequate gas service to all of the ultimate consumers who have invested many millions of dollars in gas furnaces and other gas-using equipment. Residential, commercial, and industrial consumers throughout the United States have come to rely increasingly upon this premium fuel, which in 1920 provided less than 4 percent of our total energy requirements, as compared with over 23 percent in 1953.

In the Panhandle Eastern case, decided by the Federal Power Commission in April 1954, the Commission decided that its previous ratemaking procedures with respect to pipeline company-produced gas had been unjustified since in many cases they resulted in the allowance of little or nothing for the gas produced by the pipeline company. The Commission also noted

with concern that no new major pipeline which was certificated since the Commission's previous ratemaking procedures in such cases were first established—including some of the largest systems serving enormous new markets—produces any significant portion of its total supply; and further that the ratio of pipeline produced gas to total gas transported and sold in interstate commerce has declined markedly.

The committee believes, and the Commission stated in the Panhandle Eastern case, that the interest of the public definitely lies in the direction of natural gas production by pipeline systems themselves, as distinguished from their complete dependence for gas supply upon purchases from other producers. Among the reasons for this is that such production by pipelines strengthens their bargaining position in negotiating gas purchase contracts with independent producers and by utilizing their own production to take the swings of pipeline-throughput in response to seasonal and other fluctuation of consumer demand, such pipeline systems are able to take their purchased gas at relatively uniform volumes at high load factor. They thereby generally qualify for more favorable gas purchase prices.

The Federal Power Commission has asserted that if there is to be natural-gas exploration, development, and production by pipeline systems themselves—with resultant benefits to the public—it follows that this can only result from regulatory policies which are designed to encourage, rather than to penalize, such activities.

The new subsection (f) grants the same treatment to pipeline producers as to independent producers, namely, the allowance of a reasonable market price for the gas, and thereby will encourage the pipelines to expand their production and exploration activities. The

[Page 12]

net result of this policy will be better service at lower cost to the consuming public.

There is apt precedent in the Renegotiation Act of 1943, an act which in extended or revised form has continued down to today, for the treatment hereby accorded the gas produced and

subsequently transported in interstate commerce by the natural-gas company itself.

In that act, involving the renegotiation of contracts for military procurement with the view of recapturing excessive profits, the various boards in determining the profits of an integrated company in the extractive industries included in expenses the market price, rather than the cost, of the raw material at its first extractive stage. Under the act, contracts for products of a mine, or oil or gas well, at the first form or stage in which they were customarily sold, or in which they had an established market, were excempt from renegotiation. Where the company produced the property itself, the act provided that, in determining the costs of the company, the amount it actually cost the company to produce the product should not be considered, but that instead there would be allowed as an item of cost an amount equal to what the product could have been purchased for in the first form or state in which it had an established market. For example, a producer of steel products had its renegotiated contract price with the Government and its profit determined after an expense allowance was made for the pig iron which the producer itself made and included in the ultimate product, equivalent to the "market price" for the pig iron, rather than the actual cost of pig iron in that producer's own furnaces. The same was true of oil and gas.

ADDENDUM B

H.R. 8444, 95TH CONGRESS, 1ST SESSION

SEC. 401. FINDINGS AND PURPOSES.

(a) FINDINGS.—The Congress finds that—

* * *

(4) in 1954, the Supreme Court held that the Natural Gas Act applied to the wellhead sale of natural gas in interstate commerce thereby subjecting producers selling natural gas in interstate commerce, but not those selling natural gas within the same State in which it was produced, to a regulatory standard based upon a determination of historic production costs;

* * *

SEC. 405. SALES OF OLD NATURAL GAS UNDER EXISTING CONTRACTS.

Except as provided in sections 409 and 413(e) (4), the maximum lawful price for any first sale of old natural gas produced in the United States and sold under an existing contract shall be the product of multiplying—

(1) (A) in the case of any such first sale subject to the jurisdiction of the Commission under the Natural Gas Act, the just and reasonable price established by the Commission and applicable to sales of natural gas under such contract on April 20, 1977 (without regard to any appeal of such price determination pending on April 20, 1977), or

(B) in the case of any other such first sale, the price applicable on April 20, 1977, under such existing contract; by

(2) the inflation adjustment.

* * * *

SEC. 416. JURISDICTION OF THE COMMISSION UNDER THE NATURAL GAS ACT.

(a) DEREGULATION OF CERTAIN FIRST SALES.—(1) Section 1(b) of the Natural Gas Act (15 U.S.C. 717(b)) is amended to read as follows:

"(b)(1) Except as provided in paragraph (2), the provisions of this Act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use and to natural-gas companies engaged in such transportation or sale.

"(2) The provisions of this Act shall not apply —

"(A) to any other transportation or sale of natural gas;

"(B) to the local distribution of natural gas;

"(C) to the facilities used for such distribution;

"(D) to the production or gathering of natural gas;

"(E) to any sale of natural gas to which the provisions of section 404, 406, 407, 409 or 413(e) (4) of the National Energy Act apply or to any sale or transportation of natural gas authorized by the Commission under section 414(b) of such Act; or

"(F) to any person to the extent to which such person makes a sale of natural gas to which the provisions of section 404, 406, 407, 409 or 413(e) (4) of the National Energy Act apply or to any sale or transportation of natural gas authorized by the Commission under section 414(b) of such Act".

(2) Section 2 of the Natural Gas Act (15 U.S.C. 717a) is amended by striking out subsection (6) and inserting in lieu thereof the following:

"(6) 'Natural-gas company' means a person engaged in the transportation of natural gas in interstate commerce or the sale in interstate commerce of such gas for resale, but does not include any person to the extent that such person makes a sale of natural gas to which the provisions of section 404, 406, 407, 409 or 413(e) (4) of the National Energy Act apply or makes a sale or engages in the transportation of natural gas authorized by the Commission under section 414(b) of such Act".

* * *

SEC. 417. CONFORMING AMENDMENTS TO THE NATURAL GAS ACT.

(a) AMENDMENT TO SECTION 4.— Section 4(a) of the Natural Gas Act (15 U.S.C. 717c(a)) is amended by adding at the end thereof the following new sentence: "For purposes of this section, any price for any sale of natural gas, to which the provisions of section 404, 406, 407, 409 or 413(e) (4) of the provisions National Energy Act applies, shall be deemed just and reasonable if such price does not exceed the appropriate maximum lawful price established in, or prescribed under, such provisions.".

(b) AMENDMENT TO SECTION 5.— Section 5(a) of the Natural Gas Act (15 U.S.C. 717d(a)) is amended by adding at the end thereof the following new sentence: "For purposes of this section, any price for any sale of natural gas, to which the provisions of section 404, 406, 407, 409, or 413(e) (4) of the National Energy Act applies, shall be deemed just and reasonable if such price does not exceed the appropriate maximum lawful price established in, or prescribed under, such provisions."

S. 2104, 95TH CONGRESS, 1ST SESSION

* * * *

SEC. 203. Section 1(c) of the Natural Gas Act, as redesignated by the Natural Gas Act Amendments of 1977 (15 U.S.C. 717(b)), is amended (1) by deleting "*The*" at the beginning thereof and by inserting in lieu thereof immediately after "*(c)*" the following: "(1) Except as provided in paragraph (2) of this subsection, the"; and (2) by inserting at the end thereof the following new paragraph:

"(2) Subject to the provisions of section 24 of this Act, after the date of enactment of the Natural Gas Act Amendments of 1977, the authority of the Commission to regulate the sale of natural gas to a natural-gas company for resale in interstate commerce pursuant to this Act shall cease to exist with respect to, and shall not apply to, new natural gas: Provided, That nothing contained in the Natural Gas Act Amendments of 1977 shall modify or affect the authority of the Commission in effect prior to the date of enactment of such amendments to (A) regulate the

transportation in interstate commerce of natural gas or the sale in interstate commerce for resale of old natural gas or (B) regulate the sale for resale of natural gas by any natural-gas company which transports natural gas in interstate commerce.".

* * *

SEC. 204. (a) Section 2 of the Natural Gas Act (15 U.S.C. 717(a)) is amended by redesignating paragraphs (7) through (9) as paragraphs (13) through (15), respectively, and by inserting the following new paragraphs:

* * *

"(7) 'New natural gas' means (A) natural gas sold or delivered in interstate commerce for the first time on or after January 1, 1977: Provided, however, That natural gas shall not be deemed new natural gas if the Commission finds, after hearing, that at any time prior to January 1, 1977, proper facilities were in place for natural-gas production, such natural gas could be produced economically, and such natural gas could have been sold and delivered from completed wells and was wrongfully withheld from sale or delivery: Provided further, That new natural gas contracted for sale or delivery from offshore Federal lands shall be committed for an initial contract term of not less than 15 years or for the life of the reservoir from which it is produced if less than 15 years: Provided further, That any natural gas sold or delivered in interstate commerce prior to the date of enactment of the Natural Gas Act Amendments of 1977 pursuant to limited term certificates (5 years or less) or temporary emergency contracts shall not be considered, for the purpose of this provision, as having been committed to interstate commerce, or (B) (1) natural gas produced from a reservoir discovered on or after January 1, 1977 (including a reservoir discovered by the deeper drilling of an existing well), as determined by rule by the Commission, regardless of whether or not the leases covering such newly discovered reservoirs were committed by contract or otherwise dedicated to the interstate market or (2) natural gas produced from a well or wells initiated on or after January 1, 1977, and completed within an extension of a previously discovered reservoir, as determined by rule by the Commission, regardless of

whether or not the leases covering such previously discovered reservoirs were committed by contract or otherwise dedicated to the interstate market.

"(8) 'Old natural gas' means natural gas sold or delivered in interstate commerce other than new natural gas.

* * *

SEC. 205. Section 4(e) of the Natural Gas Act (15 U.S.C. 717c(e)) is amended by adding at the end thereof the following new sentence: "Nothwithstanding the foregoing, the Commission shall have no power to deny, in whole or in part, any rate or charge made, demanded, or received by any natural-gas company for, or in connection with, the purchase or sale of natural gas, or that portion of the rates and charges of such natural-gas company which relates to such purchase or sale, except (A) to the extent that such rates or charges, or such portion thereof, for new natural gas sold or delivered from offshore Federal lands exceed the national ceiling or interim ceiling established or modified by regulation of the Commission pursuant to section 24 of this Act or (B) in any case where a natural-gas company which transports natural gas in interstate commerce purchases new natural gas from an affiliate or produces new natural gas from its own properties, to the extent that the Commission determines that the rates and charges therefor exceed the current rates and charges, or portion thereof, made, demanded, or received for comparable sales by persons not affiliated with such natural-gas company.".

* * *

SEC. 206. Section 5(a) of the Natural Gas Act (15 U.S.C. 717d(a)) is amended by striking the period at the end thereof and by adding the following: " : Provided further, That the Commission shall have no power (1) to deny, in whole or in part, any rate or charge made, demanded, or received by any natural gas company for, or in connection with, the purchase or sale of new natural gas, or that portion of the rates and charges of such natural-gas company which relates to such purchase or sale except (A) to the extent that such rates or charges, or such

portions thereof, for new natural gas sold or delivered from offshore Federal lands exceed the national ceiling or interim ceiling established or modified by regulation of the Commission pursuant to section 24 of this Act, or (B) in any case where a natural-gas company which transports natural gas in interstate commerce purchases new natural gas from an affiliate or produces new natural gas from its own properties, to the extent that the Commission determines that the rates and charges therefor exceed the current rates and charges, or portion thereof, made, demanded, or received for comparable sales by persons not affiliated with such natural-gas company; or (2) to order a decrease in the rate or charge made, demanded, or received for the sale or transfer of old natural gas or new natural gas produced from offshore Federal lands by a natural-gas company if such rate or charge has been previously determined or deemed to be just and reasonable pursuant to this Act.".

* * *

SEC. 209. The Natural Gas Act, as amended by the Natural Gas Act Amendments of 1977, is further amended by adding at the end thereof the following six new sections:

* * *

"SEC. 24. (a)(5) From and after January 1, 1982, there shall be no ceiling price applicable to the sale or delivery of new natural gas from offshore Federal lands.

* * *

"(b) (2) From and after two years subsequent to the date of enactment of the Natural Gas Act Amendments of 1977, there shall be no ceiling price applicable to the sale or delivery of new natural gas from sources other than offshore Federal lands.

ADDENDUM C

NATURAL GAS POLICY ACT OF 1978, 15 U.S.C. §§ 3301, *et seq.*

SECTIONS 2(20), 2(21) and 2(22), 15 U.S.C. § 3301(20), (21), and (22))

SEC. 2. DEFINITIONS.

* * *

(20) SALE.— The term "sale" means any sale, exchange, or other transfer for value.

(21) FIRST SALE.—

(A) GENERAL RULE.—The term "first sale" means any sale of any volume of natural gas—

(i) to any interstate pipeline or intrastate pipeline;

(ii) to any local distribution company;

(iii) to any person for use by such person;

(iv) which precedes any sale described in clauses (i); (ii), or (iii); and

(v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this Act.

(B) CERTAIN SALES NOT INCLUDED.— Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

(22) DELIVER.— The term "deliver" when used with respect to any first sale of natural gas, means the physical delivery from the seller; except that in the case of the sale of proven reserves in place to any interstate pipeline, any intrastate pipeline, any local distribution company, or any user of such natural gas, such term means the transfer of title to such reserves.

* * *

SECTION 501(a) and (b), 15 U.S.C. § 3411(a) and (b)

SEC. 501. GENERAL RULEMAKING AUTHORITY.

(a) IN GENERAL.— Except where expressly provided otherwise, the Commission shall administer this Act. The Commission, or any other Federal officer or agency in which any function under this Act is vested or delegated, is authorized to perform any and all acts (including any appropriate enforcement activity), and to prescribe, issue, amend, and rescind such rules and orders as it may find necessary or appropriate to carry out its functions under this Act.

(b) AUTHORITY TO DEFINE TERMS.— Except where otherwise expressly provided, the Commission is authorized to define, by rule, accounting, technical, and trade terms used in this Act. Any such definition shall be consistent with the definitions set forth in this Act.

SECTION 601(b)(1)(A) & (E), 15 U.S.C. § 3431(b)(1)(A) & (E)

(b) CHARGES DEEMED JUST AND REASONABLE.—

(1) SALES.—

(A) FIRST SALES.—Subject to paragraph (4), for purposes of sections 4 and 5 of the Natural Gas Act, any amount paid in any first sale of natural gas shall be deemed to be just and reasonable if—

(i) such amount does not exceed the applicable maximum lawful price established under title I of this Act; or

(ii) there is no applicable maximum lawful price solely by reason of the elimination of price controls pursuant to subtitle B of title I of this Act.

* * *

(E) AFFILIATED ENTITIES LIMITATION.— For purpose of paragraph (1), in the case of any first sale between any interstate pipeline and any affiliate of such pipeline, and amount paid in any first sale shall be deemed to be just and reasonable if, in addition to satisfying the requirements of such paragraph, such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.

SECTION 601(c)(2)(A), 15 U.S.C. § 3431(c)(2)(A)

(c) GUARANTEED PASSTHROUGH.—

* * *

(2) RECOVERY OF JUST AND REASONABLE PRICES PAID.— For purposes of sections 4 and 5 of the Natural Gas Act, the Commission may not deny any interstate pipeline recovery of any amount paid with respect to any purchase of natural gas if—

(A)) under subsection (b) of this section, such amount is deemed to be just and reasonable for purposes of sections 4 and 5 of such Act, and

Supplemental Petitioner's Brief

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Nos. 81-1889, 81-1958,
81-2042 and 82-19

IN THE

Supreme Court of the United States

OCTOBER TERM 1982

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK; ARIZONA ELECTRIC POWER COOPERATIVE, INC.; STATE OF MICHIGAN; AND FEDERAL ENERGY REGULATORY COMMISSION,
Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

**ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT**

MOTION OF ARIZONA ELECTRIC POWER COOPERATIVE, INC. FOR DIVISION OF ORAL ARGUMENT TIME

No. 81-1958

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

Public Service Commission of the State of New York,	
Arizona Electric Power Cooperative, Inc.,	
State of Michigan,	
Federal Energy Regulatory Commission, *Petitioners,*	Nos. 81-1889, 81-1958, 81-2042, 82-19
v.	
Mid-Louisiana Gas Company, *et al.,* *Respondents.*	

MOTION OF ARIZONA ELECTRIC POWER COOPERATIVE, INC. FOR DIVISION OF ORAL ARGUMENT TIME

Petitioner, Arizona Electric Power Cooperative, Inc. (AEPCO), hereby moves the Court to allocate to its counsel 15 minutes of the oral argument time alloted to petitioners.[1] This division is necessary becaue AEPCO is the only petitioner which will argue certain dispositive issues which were not part of the rationale for the Commission Orders under review and were not addressed in the decision of the Court below. The rationale AEPCO will argue presents an independent basis for decision by this Court which is unusually simple and strong. AEPCO has set forth this basic rationale in its brief (pp. 14-27). No other party has done so.

[1]The Commission is willing to relinquish time to a unanimously designated counsel representing other petitioners. AEPCO and New York have been unable to agree. Michigan does not wish to present argument.

The Commission and the New York Commission have cast this case in the mold of a dispute concerning the proper interpretation of the definition of a "first sale" under the NGPA. AEPCO has cast this case in the wholly different mold of whether the power to regulate a pipeline's different mold of whether the power to regulate a pipeline's own gas production on a "cost of service" basis which the Commission has enjoyed for four decades under the Natural Gas Act (NGA) have been repealed by the "unless" clause of the "first sale" definition in Section 2(21) of the NGPA as the Court below erroneously held.

AEPCO argues that Sections 4 and 5 of the NGA grant the Commission the power to fix just and reasonable rates for pipelines. Such power has always been held to include the fixing of rates for a pipeline's own production on a cost of service basis. *Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581 (1945). It is undisputed that the NGPA does not expressly repeal this NGA authority of the Commission. The Court below held that because "...the Commission lacked authority to set prices for interstate pipeline production under the NGA... the price for pipeline production will now be set under the NGPA" (App. A-15). Thus, in essence, the Court below held that the NGPA had impliedly repealed the Commission's authority to set cost of service rates for a pipelines' own production, but did not address the question of whether the legal requirements for a repeal by implication were satisfied here. In fact, those requirements are not met here. There is *no* expression of Congressional intent to repeal. There is *no* showing, or even claim, of irreconcilable conflict between the two statutes. Worse still, the Court did not justify its holding by these traditional indicia of a repeal by implication.

AEPCO respectfully submits that its lines of argument against an implied repeal (Br., pp. 14-27) are sufficiently relevant and strong to warrant their oral presentation to this Court and that unless it is granted the requested time, the Court will be deprived of the benefit of oral argument on this crucial issue.

Respectfully submitted,

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Petitioner's Brief

3

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No. 81-2042

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

STATE OF MICHIGAN

Petitioner,

v.

MID-LOUISIANA GAS COMPANY, et. al.,

Respondents.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT
OF APPEALS FOR THE FIFTH CIRCUIT

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QUESTION PRESENTED FOR REVIEW

Does the act of commingling natural gas produced by a pipeline company with natural gas purchased from others for resale, constitute a "first sale" under the Natural Gas Policy Act of 1978, when such commingling is not accompanied with any of the indicia normally associated with a "sale"?

PARTIES BELOW

The following is a list of all parties to the case below:

American Gas Association
Arizona Electric Power Cooperative and
City of Wilcox
Colorado Interstate Gas Company
Columbia Gas Transmission Corporation
Consolidated Gas Supply Corporation
Kansas-Nebraska Natural Gas Company
Mid-Louisiana Gas Company
Natural Gas Pipeline Company of America
Northwest Pipeline Corporation
Southern Natural Gas Company
Kentucky-West Virginia Natural Gas Company
Northern Natural Gas Company
The Public Service Commission of Wisconsin
The State of Michigan and the Michigan Public
Service Commission
The Public Service Commission of the State of New York
United Gas Pipeline Company
El Paso Natural Gas Company
Michigan Wisconsin Pipe Line Company
Kansas State Corporation Commission

TABLE OF CONTENTS

	Page
Question Presented For Review	i
Parties Below	ii
Table of Contents	iii
Table of Authorities	iv
Opinions and Orders Below	1
Jurisdiction	2
Statutes Involved	2
Statement of the Case	3
I. Introduction	3
II. Regulatory Background	4
III. The NGPA and the Concept of "First Sale"	6
Summary of Argument	7
ARGUMENT	9
I. Congress Intended To Preserve State Regulatory Authority, But The Decision Of The Court Below Abolished Price Regulation of Intrastate Production	9
II. Intracorporate Transfers Do Not Meet The Section 2(21) Definition of "First Sale," Because They Are Not Transfers For Value Within The Section 2(20) Definition of "Sale"	11
III. The Court Below Violated Commonly Accepted Canons of Statutory Construction	15
IV. The Decision Below Results In Inequitable Windfalls To The Pipelines	22
Conclusion	27

TABLE OF AUTHORITIES

STATUTORY AUTHORITY Page

Natural Gas Act of 1938, 15 U.S.C. §717, et. seq. 4

Natural Gas Policy Act of 1978,

15 U.S.C. §3301(20) 1, 2, 3, 8, 12

15 U.S.C. §3301(21) 2, 3, 7, 8

15 U.S.C. §3301(21)(B) 6

15 U.S.C. §3311(b)(9) 19, 21

15 U.S.C. §3343 19

15 U.S.C. §3411 .....6, 19

15 U.S.C. §3416(b) 7

15 U.S.C. §3432(a) 10

CASE AUTHORITY

A. Federal

Batterton v. *Francis*, 432 U.S. 416, 425 (1977) 20

California v. *Zook*, 336 U.S. 725 (1949) 11

Columbia Gas Development Corp. v. *Federal Energy Regulatory Commission*, 651 F.2d 1146 (1981) 22

Commission of Internal Revenue v. *Feihofer*, 102 F.2d 787, 789 (3rd cir., 1939) 13

Democratic Central Committee of District of Columbia v. *Washington Metropolitan Area Transit Commission*, 485 F.2d 786 (D.C. cir., 1973) 17

ECEE, Inc. v. *Federal Energy Regulatory Commission*, 611 F.2d 554 (5th Cir., 1980) 22

Ford Motor Credit Co. v. *Milhollin*, 444 U.S. 555, 565 (1980) 18

Haig v. *Agee*, 453 U.S. 280, 300 (1981) 18

Head v. *Board of Examiners*, 374 U.S. 424 (1963) 11

Page

Helvering v. *Nebraska Bridge Supply and Lumber Co.*, 115 F.2d 288, 290 (8th cir., 1940) 13

Herweg v. *Ray*, ... U.S. ...., 716 L.Ed. 2d 137, 102 S.Ct. .... (1982) 20

Jones v. *Rath Packing Co.*, 430 U.S. 518; 97 S.Ct. 1305; 57 L.Ed. 604 (1977) 11

Mid-Louisiana Gas Company, et. al. v. *Federal Energy Regulatory Commission*, 664 F.2d 530 .....1, 9, 19

Montana Power Co. v. *Federal Energy Regulatory Commission*, 599 F.2d 295 (9th Cir, 1979) 17

Phillips Petroleum v. *Wisconsin*, 347 U.S. 674 (1954) 4

Piper v. *Chris-Craft Industries, Inc.*, 430 U.S. 1, 26 (1977) 20

Posadas v. *National City Bank*, 296 U.S. 497 (1936) 17

Schweiker v. *Gray Panthers*, 453 U.S. ...., 69 L.Ed 2d 460, 101 S. Ct. (1981) 20

Standard Bank of Canada v. *Lowman*, 1 F.2d 935, (W.D. Wa., 1924) 13

Tenneco Oil Co v. *Federal Energy Regulatory Administration*, 613 F.2d 298, 302 (Temp. Emerg. Cir., 1979) 15

United States v. *American Trucking Assoc.*, 310 U.S. 534 (1939) 16, 18

United States v. *Atherton*, 561 F.2d 747 (9th cir., 1977) .. 13

United States v. *United Continental Tuna*, 425 U.S. 164 (1976) 17

B. State Page

Coulter Electronics v. *Department of Revenue*, 365 So. 2d 806 (Fla. App., 1978) 13

Morehead v. *Harris*, 262 N.C. 330, 137 S.E. 2d 174 (1964) 13

North Shore University Hospital v. *D'Elia*, 79 A.D.2d 606, 433 N.Y.S. 2d 495 (1980) 13

MISCELLANEOUS

Black's Law Dictionary (5th ed.) 12, 13

No. 81-2042

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

STATE OF MICHIGAN

Petitioner,

v.

MID-LOUISIANA GAS COMPANY, et. al.,

Respondents.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT
OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR PETITIONER

The State of Michigan (Michigan) petitioned for and was granted a Writ of Certiorari to review the December 23, 1981 decision of the United States Court of Appeals for the Fifth Circuit in *Mid-Louisiana Gas Company, et. al.* v. *Federal Energy Regulatory Commission*, Case No. 80-3804. The decision vacated Orders Nos. 58, 98 and 102 issued by the Federal Energy Regulatory Commission (FERC) on November 14, 1979, August 4, 1980 and October 3, 1980, respectively, because of the court's interpretation of Section 2(21) of the Natural Gas Policy Act of 1978, 15 U.S.C. §3301(21).

OPINIONS AND ORDERS BELOW

The Opinion of the United States Court of Appeals for the Fifth Circuit is reported at 664 F.2d 530. The FERC orders are unreported, but are contained in the Joint Appendix now shared by Petitioners and Respondents, and filed with the Peti-

tion For Writ of Certiorari of the Public Service Commission of the State of New York (NYPSC) dated April 12, 1982 in Docket No. 81-1889.

JURISDICTION

The United States Court of Appeals for the Fifth Circuit entered judgment in this matter on December 23, 1981. In an order dated January 11, 1982, the court extended the time for rehearing until January 20, 1982. Petitions for rehearing filed by Michigan, the NYPSC and Arizona Electric Power Cooperative, Inc. were denied February 5, 1982. Michigan then filed its Petition for Writ of Certiorari within the time limits of 28 U.S.C. §2101(e), invoking this court's jurisdiction under 28 U.S.C. §1254(1). The petition was granted in an order dated October 4, 1982.

STATUTES INVOLVED

Consideration of the decision of the United States Court of Appeals for the Fifth Circuit involves Sections 2(20) and 2(21) of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. §§3301(20) and (21). Those sections read as follows:

> "(20) Sale.—the term 'sale' means any sale, exchange, or other transfer for value." 15 U.S.C. §3301(20).
>
> "(21) First Sale.—
>
> (A) General rule.—The term 'first sale' means any sale of any volume of natural gas—
>
> (i) to any interstate pipeline or any intrastate pipeline;
>
> (ii) to any local distribution company;
>
> (iii) to any person for use by such person;

(iv) which precedes any sale described in (i), (ii), (iii);

(v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) as is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this chapter.

(B) Certain sales not included.—Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local gas distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof." 15 U.S.C. §3301(21).

STATEMENT OF THE CASE

I.

Introduction

Michigan seeks review of a decision of the United States Court of Appeals for the Fifth Circuit, which brought more than 40 years of pipeline regulation at the federal level to an abrupt halt and severely affected state regulation of natural gas production without explicit statutory authority. The Court by its decision, accorded "first sale" status to an intracorporation transfer of natural gas (commingling of two sources) between a fictional production division and transportation division, without the transfer being one "for value" as required by the definition of "sale" in NGPA §20, 15 U.S.C. 3301(20). In doing so, the court judicially established a fictional transaction

based upon a statutory interpretation that does not manifest congressional intent and that is directly contrary to an express statutory provision.

II.

Regulatory Background

Since the inception of regulation in 1938 under the Natural Gas Act (NGA), 15 U.S.C. §717 et. seq., the Federal Power Commission and its successor the FERC have regulated the cost of pipeline natural gas production included in the pipeline customers' rates. This was done on a cost-of-service basis by either capitalizing or expensing production costs, regardless of the success or failure of the production efforts. Therefore, most of the risk of failure was eliminated from pipeline production operations, since the pipeline earned a fair return on all prudent production investment.

In 1969 the commission concluded, after years of hearings in pipeline production area rate proceedings, that pipeline production from leases acquired after October 9, 1969, would be priced at the appropriate "area" rate applicable to sales of gas by independent producers, and it also applied the area rate to pipeline production sold "off system" at the wellhead to other pipelines. The area rate was not applicable to pre-October 9, 1968 production, and certain pipelines were allowed, at their request, to price production from newer leases on a cost-of-service basis, because it resulted in the most financially advantageous rates for the pipeline. However, cost-of-service pricing of these leases became unfavorable with passage of the NGPA, resulting in this litigation.

Quite different, however, is the history of regulating independent natural gas producers. Prior to this Court's decision in *Phillips Petroleum* v. *Wisconsin*, 347 U.S. 672 (1954), the

commission exercised no jurisdiction over sales of natural gas to pipelines by independent producers. After the *Phillips* decision, regulation of independent producer prices resulted in "area" rates, followed by "nationwide" rates.[1] These rates were based primarily on average industry historical costs for flowing gas, and unit rates were applied to each Mcf of gas sold. The risk of failure in production efforts was placed upon independent producers; opposite of the situation then existing with pipeline production.

Federal regulation over independent natural gas producers has been in controversy ever since the *Phillips* case. Twice during the 1950's Congress enacted legislation limiting such regulation, but both bills were vetoed. Each bill expressly addressed pipeline production as well; the first bill excluded pipeline production from deregulation and the second bill specified that pipelines would be allowed the reasonable market price as a part of their cost-of-service for any gas produced.[2]

Producer regulation became an active issue again in the 1970's when curtailment of pipeline service occurred, stemming from inadequate supplies in the interstate market. Many conflicting proposals were considered, from complete deregulation to federal control of all sales in the intrastate market. The compromise legislation which became the NGPA was before Congress for more than two years, but during that time no sponsor of the legislation expressed any dissatisfaction with existing regulation of pipeline production, as contrasted with regulation of producer production.

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[1]

See, *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968).

[2]

See, H.R. 1758, 81st Cong., 2nd Sess., vetoed April 15, 1980, House Doc. No. 555, 81st Cong., 2nd Sess. and H.R. 6645, 84th Cong., 2nd Sess., vetoed February 17, 1956, House Doc. No. 342, 84th Cong., 2nd Sess.

III.

The NGPA and the Concept of "First Sale"

The NGPA does not expressly exempt pipeline production from regulation. Rather it provides eight major categories of "maximum lawful" ceiling prices applicable to "first sales" of natural gas. A "first sale" is the "*sale*" of any volume of gas *to* an interstate or intrastate pipeline, local distribution company or end user, expressly excluding any sale *by* an interstate or intrastate pipeline, local distribution company or affiliate thereof "unless such sale is attributable to volumes of natural gas produced by [it] . . . ." 15 U.S.C. §3301(21)(B). Nothing in the legislative history provides any further elucidation of this language. However, the FERC is delegated authority in Section 501, 15 U.S.C. §3411, to issue rules and to further define the terms used in the act.

In Order No. 58 the FERC adopted a rule which concluded that the only sales "attributable" to pipeline production were those contracted for at the wellhead, rather than the larger share of pipeline production which is commingled with gas purchased by the pipeline for resale to distribution companies or direct sales customers. Effectively then, Order No. 58 meant all production commingled with purchases would remain subject to the commission's pricing jurisdiction under the NGA.

Order No. 58 was followed 9 months later by Order No. 98, amending the commission's regulations under the NGA, as an exercise of discretion, to price all pipeline production that did not already qualify for the NGPA prices under Order No. 58, at the applicable NGPA ceiling rates for independent producer sales, unless that gas was currently being priced on a cost-of-service basis due to the pipeline's earlier election. Order No. 102, issued 2 months after Order No. 98, denied petitions for rehearing filed by a number of parties.

Several pipelines then took separate appeals of both FERC orders to the United States Court of Appeals for the Fifth Circuit, based on Section 506(b) of the NGPA, 15 U.S.C. §3416(b). Those appeals of Order No. 58, as affirmed by Order No. 102, were styled *Mid-Louisiana* v. *FERC*, No. 80-3804. Michigan intervened in No. 80-3804 supporting the FERC. The Fifth Circuit's decision and petitions for rehearing followed, as discussed above. Thereafter, Michigan filed a timely petition for a writ of certiorari[3] which was granted October 4, 1982.

SUMMARY OF ARGUMENT

This case presents considerations of first impression important to the nation's energy policy, i.e., whether 40 years of federal regulation of interstate pipeline production and even more years of state regulation of production by intrastate pipelines and local distribution companies should be ignored in favor of a judicially created fictional transaction. The United States Court of Appeals for the Fifth Circuit concluded that gas produced by a pipeline company is transferred from the production division to the transportation division of the pipeline. This so-called transfer is actually only a commingling of pipeline produced gas with pipeline purchased gas. Moreover, the court held that such a fictional transfer was a "first sale" within NGPA, §2(21), 15 U.S.C. §3301(21). Michigan submits the decision of the Fifth Circuit is erroneous, because it (1) judicially puts an end to price regulation, at both the federal and state levels, of natural gas production by interstate pipelines, intrastate pipelines, and local distribution companies without those matters having been addressed by Congress, (2) judicially creates a fictional transaction which has no basis in fact, and directly contradicts a specific statutory provision, (3) is based upon the incorrect assumption that no valid reason

[3] See, 28 U.S.C. §2101(c).

exists to distinguish between independent producers and pipelines, and (4) provides the pipelines with windfall gains at the consumers' expense.

The Fifth Circuit's decision qualifies all production for NGPA ceiling prices, regardless of whether such production is by interstate pipelines, intrastate pipelines or local distribution companies regulated by the states. The Court's holding was made without any suggestion that Congress intended such a result. In fact, the NGPA itself expressly reserves state authority. Thus, the Court of Appeals decision is clearly erroneous because it contradicts NGPA provisions and violates rudimentary rules of statutory construction disfavoring pre-exemption of state regulation without clear Congressional intent to do so.

Similarly, the decision of the Court of Appeals ended decades of regulation over pipeline production without Congressional consent. Generally speaking, the NGPA governs sales to pipelines. It contains no express exemption of pipeline production from regulation, but it is expressly inapplicable to sales by pipelines "unless such sale is attributable to volumes of natural gas produced by [it] . . . ." Nevertheless, the Fifth Circuit found that the act of commingling pipeline production with natural gas purchases made by the pipeline constitutes a transfer and a "first sale" under the NGPA, §2(21). However, this act of commingling has none of the indicia of a "sale" required by §2(20) of the NGPA. Therefore, the Court of Appeals decision is clearly erroneous, because it contradicts yet another NGPA provision, creates a judicial fiction having no basis in fact, and violates the rules of statutory construction disfavoring repeals by implication and judicial activism in instances where Congressional silence constitutes considered abstention.

The decision below incorrectly assumes there is no valid reason to distinguish between independent producers and pipe-

lines. However, these separate entities have been treated differently, because of valid distinctions in historic development of regulation and consequent advantages conferred upon pipelines, not otherwise available to independent producers. The FERC retained these distinctions, because abolishing them would result in windfalls to the pipelines and it was in the consumers' best interests to retain the historical relationships. However, the court below swept away these distinctions without considering the legitimate bases for them, shifting the pricing burden to the consumer who financed pipeline production investment and bore the risk associated therewith, from the pipeline who thus enjoys an inequitable windfall because it made no investment and bore no risk.

ARGUMENT

I.

Congress Intended To Preserve State Regulatory Authority, But The Decision Of The Court Below Abolished Price Regulation Of Intrastate Production

The Fifth Circuit's opinion states:

> '. . . [W]e hold that Congress *clearly* intended for *any* production attributable to an 'interstate pipeline, intrastate pipeline or local distribution company, or any affiliate thereof', to be accorded first sale status under the NGPA and that Congress contemplated that the intracorporate transfer of pipeline production to the pipeline would be treated as a first sale." 664 F.2d 530, 538. (Emphasis supplied)

The decision thus qualifies all production for NGPA ceiling prices, whether produced by interstate pipelines, intrastate pipelines or local distribution companies previously regulated by the various states. This broad holding was made without any suggestion in the lengthy legislative history of the NGPA that Congress intended to end state regulation, or that such state regulation was a significant element of the dual market problem created under the NGA when producers sold their gas in the unregulated intrastate markets rather than in the regulated interstate market. The NGPA imposed regulation for the first time upon sales by producers to intrastate customers, but there is nothing in it to indicate an intention to preempt existing state regulation over the cost of gas produced by intrastate pipelines and local distribution companies. In fact Section 602(a), 15 U.S.C. §3432(a), expressly reserves state authority to prescribe maximum rates lower than those authorized by "first sales".

Section 2(21) is applicable to production efforts of intrastate pipelines and local distribution companies, as well as those of interstate pipelines. However, prior to the Fifth Circuit decision in this case, intrastate entities were left to state regulation under §602(a) of the NGPA and §1(b) of the NGA. Nevertheless, the Court below adopted a position completely contrary to §602(a) and §1(b). It said production by intrastate pipelines and local distribution companies is entitled to be accorded "first sale" status under the NGPA.

Prior to this decision, state regulatory commissions were free to treat intrastate production in any reasonable manner consistent with their enabling legislation. Now they are precluded from applying any cost-of-service methodology (Michigan is a cost-of-service jurisdiction for intrastate production) to an intrastate pipeline's or local distribution company's production operations which would result in rates lower than those authorized by "first sales."

Assuming Congress could preempt state regulation over the production operations of intrastate pipelines and distribution companies, there is no indication whatsoever that it intended to supersede state regulation by application of the NGPA pricing provisions to independent producers. State authority was afforded continuing protection by §602(a) of the NGPA and §1(b) of the NGA. In such a case preemption should not be assumed, absent clear indication of Congressional intent. *Head* v. *Board of Examiners*, 374 U.S. 424 (1963); *California* v. *Zook*, 336 U.S. 725 (1949).

> "Where . . . the field which Congress is said to have preempted has been traditionally occupied by the States . . . 'we start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.'" *Jones* v. *Rath Packing Co*, 430 U.S. 518, 525; 97 S.Ct. 1305; 57 L.Ed.2d 604 (1977).

The Court of Appeals has clearly disregarded this principle of statutory construction, and in the process it cut short a lengthy history of state regulation over intrastate production.

II.

Intracorporate Transfers Do Not Meet The Section 2(21) Definition of "First Sale", Because They Are Not Transfers for Value Within The Section 2(20) Definition of "Sale"

The lower court's opinion assumes that every interstate pipeline has a distinct "production division" and "transportation division". While it is certainly useful to an understanding of the court's opinion to use this terminology herein, there is no real indication anywhere that pipelines have such distinct divisions. What actually happens is that the pipelines have both produced gas and purchased gas for sale to their customers.

Gas from these sources is commingled before sale in most cases. In Order No. 58 the FERC said sales from this commingled stream were not "first sales" under the NGPA. Nevertheless, the Fifth Circuit labeled the commingling of sources as a transfer, called it a "first sale", and vacated Order No. 58. Thus, not only is the transfer itself a judicially created fictional transaction, but the arbitrary division by the lower court of a single entity into two distinct parts is also artificial.

The issue focused upon by the FERC in Order No. 58 and by the parties in the court below was whether sales to distribution companies and end users "downline" from the wellhead were "first sales" under Section 2(21) of the NGPA. However, the lower court reached its decision by focusing upon the fictional intracorporate transfer (commingling) as a first sale, imputing a sale at the wellhead from the pipeline to itself. The court thus eliminated the necessity to consider problematical policy and regulatory issues in the analysis of downline sales. It also made inapplicable an impressive arrary of legislative history assembled by the FERC, suggesting Congress intended NGPA prices to apply only to wellhead sales rather than downline sales.[4]

The holding of the lower court that Section 2(21) "clearly" accorded first sale status to all pipeline production is just as *clearly* erroneous. The NGPA contains a simple and straightforward definition of "sale" in Section 2(20), 15 U.S.C. §3301(20), requiring a sale to be at the very least a "transfer for value." For an NGPA sale to exist there must therefore be a transfer of natural gas in exchange for something else of value. A "transfer" is a passing of property from one person to another. Black's Law Dictionary (5th ed.) p. 1342. A "transfer for value" constitutes a sale only when title to prop-

[4]

These policy issues and legislative history are discussed in the FERC brief in 80-3804. The pertinent portion thereof was an appendix to Michigan's petition in this case.

erty passes from one to another for valuable consideration. "Where a transfer of property takes place without the transferor's receiving anything of value for the property transferred, the transaction is not a sale or exchange." *Helvering* v. *Nebraska Bridge Supply and Lumber Co.*, 115 F.2d 288, 290 (8th cir., 1940). See, *Commission of Internal Revenue* v. *Feihofer*, 102 F.2d 787, 789 (3rd cir., 1939).

The necessity for consideration in the transfer, or exchange for value, is not only implicit in Congressional use of the word "transfer", it is made mandatory by employing the term "for value." Value is any consideration sufficient to support a simple contract. *Standard Bank of Canada* v. *Lowman*, 1 F.2d 935 (W.D. Wa., 1924). Value also means valuable consideration. *Morehead* v. *Harris*, 262 N.C. 330, 137 S.E. 2d 174 (1964). "The term [value] is often used as an abbreviation for 'valuable consideration', especially in the phrases 'purchase for value', 'holder for value', etc." Black's Law Dictionary (5th ed) p. 1391. The term "transfer for value" is a like phrase and should be construed the same; as requiring consideration.

Furthermore, a "transfer" cannot exist when a single entity transacts with itself. For example, it has been held that a change in ownership of property held as joint tenants by two individuals, to ownership by a corporation in which the same individuals were sole principals, is not a transfer. *North Shore University Hospital* v. *D'Elia*, 79 A.D.2d 606, 433 N.Y.S. 2d 495 (1980). Similarly, inter-corporate transactions between parent and subsidiary corporations are not sales, when no invoices are prepared, no payments made, and no delivery; only internal accounting entries. *Coulter Electronics* v. *Department of Revenue*, 365 So.2d 806 (Fla. App., 1978). Also, the judicially created "first sale" doctrine in copyright cases requires a divestiture of the copyright to someone else, and only then is the right to vend that copyright lost. *United States* v. *Atherton*, 561 F.2d 747 (9th cir., 1977). The same

rationales hold true in this case. It is logical to require an actual transfer to someone else before you call the transaction a first sale. There can be no first sale to yourself, and accounting entries are themselves insufficient to constitute a transfer.

Intracorporate transfers of pipeline natural gas production to the pipeline, if they actually exist, are not attended with any of the indicia commonly associated with a natural gas sale, or transfer for value. No contract is signed, no invoices prepared, no payments made, no certificate of public convenience and necessity issued, no formal structure to the arrangement, no rights to be bargained, no give and take, no consideration, and nothing of value is transferred. The gas itself has value, but no valuable rights to that gas pass, and nothing is given to or by the pipeline in exchange. There is only a commingling of two different sources of gas. It cannot even be said that control over the gas passes, because the individual divisions, if they exist in a given pipeline, have no right to exercise independent control; they act only for the benefit of the pipeline as a whole. These transactions are not recorded as sales on the pipeline's books, and they do not result in collection of any revenue, taxable or otherwise. In short the transfer exists, if at all, only as accounting entries on the internal books and records of the pipeline as a single entity, and it should not be treated as anything more. The commission recognized the mere accounting nature of the internal transfer and in its brief to the lower court said: "It is simply not a sale at all."[15] The FERC's statement is true because an intracorporate transaction is neither a transfer from one to another, nor does it pass anything of value.

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[15] No. 80-3804, FERC brief, p. 32.

III.

The Court Below Violated Commonly Accepted Canons Of Statutory Construction

While the Fifth Circuit directed the FERC in this case to treat intracorporate transfers as sales, another court did not do so, because such transfers are inconsistent with a sale. In an opinion impliedly based on the considerations in the paragraph immediately above, a temporary emergency court of appeals said:

> "The first principle of regulatory construction is that regulatory terms must be interpreted according to their commonly understood definitions in the absence of a specific regulatory definition. *Burns* v. *Acala*, 420 U.S. 575 (1975); *Addison* v. *Holly Hill Fruit Products*, 322 U.S. 607 (1944). The commonly understood meaning of a 'sale' is a *transfer of title* in return for valuable consideration. *Commissioner of Internal Revenue* v. *Brown*, 380 U.S. 563 (1965). The FEA cites no cases that are to the contrary. To hold that a 'sale' may occur simply in the receipt of value from property would be to rob from the term any legal or economic significance. See *Mobil Oil Corp.* v. *Federal Power Commission*, 463 F.2d 256, 262-63 (D.C. Cir.) *cert. denied*, 406 U.S. 976 (1972)" *Tenneco Oil Co* v. *Federal Energy Administration*, 613 F.2d 298, 302 (Temp. Emerg. Cir., 1979).

Further, the term "transfer for value" relates to a sale "*by* any interstate pipeline," not a sale to a pipeline. The obvious meaning of the entire clause is that, when gas is produced at a distant point from the pipeline's transportation system for example, pipeline production sold at the wellhead to a second party enjoys "first sale" status. Nothing about the "unless" clause legitimately lends any credence to the intracorporate transaction theory. In fact the natural and expected meaning

of the "unless" clause supports a completely different interpretation.

A "sale" was not defined by Congress in Section 2(20) to include intracorporate transfers or transfers without value, such as commingling two sources of gas. However, the lower court opinion glossed over this omission in the statute, pointed out to it by the FERC. This controlling issue was only mentioned on the very last page of the opinion, and the court then ignored it, without discussing the Section 2(20) definition of "sale". Had the court considered the Section 2(20) definition of "sale", it could only have concluded that intracorporate transfers (commingling) are not first sales, because they are not transfers for value.

While Michigan does not suggest the entire meaning of "first sale" is plain, the definition of the word "sale" is clear. When Congress defines a term in an unambiguous fashion, it is not generally subject to interpretation by the courts. *United States* v. *American Trucking Assoc.*, 310 U.S. 534 (1939). Nevertheless, the plain meaning of a term or provision in a statute is not controlling when it "produces[s] absurd results . . . 'plainly at variance with the policy of the legislation as a whole'. . . ." 310 U.S. 534, 543, *supra*. On occasion, courts follow the purpose behind a statute rather than its literal words, when Congressional intent is ambiguous.

However, it is clear in this case that Congress did not expressly include pipeline production under the NGPA. Therefore, the unambiguous definition of "sale" is controlling, since it is not at variance with any explicit NGPA policy regarding pipeline production. Likewise, the stated NGPA policy respecting independent producers should not be applied by the court to pipelines.

To hold otherwise, as the court below did, creates a repeal by implication of pipeline regulation under the NGA; an

action not favored by this court. *Posadas* v. *National City Bank*, 296 U.S. 497 (1936); *United States* v. *United Continental Tuna*, 425 U.S. 164 (1976). Furthermore, the lower court's holding violates the well settled regulatory principle that right to gain follows risk of loss. *Democratic Central Committee of District of Columbia* v. *Washington Metropolitan Area Transportation Commission*, 485 F.2d 786 (D.C. cir., 1973). Pipelines have not had to bear the risks of production and should not receive the gain associated with NGPA prices, especially when they earlier elected cost-of-service pricing because it was then beneficial. Moreover, regulation must relieve consumers from bearing more than their fair share of utility costs when competitive forces do not provide that protection. *Montana Power Co.* v. *Federal Energy Regulatory Commission*, 599 F.2d 295 (9th Cir, 1979). The FERC's interpretation of the statute preserves these considerations, while the lower court ignored them.

Congressional intent to actually exclude pipeline production from the NGPA at least to the extent embodied in FERC Order No. 58, is shown by the House Report on the President's proposed National Energy Act in the form of H.R. 6831, which provided:

> "The Committee intends that the term 'first sale' be applied by the Federal Power Commission to the first transfer of natural gas for value *in an arms-length transaction*." H. Rep. 95-496, Part. 4, 95th Cong. 1st Sess. (1977), p. 103. *reprinted in* 1978 U.S. Code Cong. & Ad. News 85470. (Emphasis Supplied)

There is no arms-length transaction involved in an intracorporate transfer of pipeline natural gas to the pipeline. The transaction is wholly within the parent pipeline, and cannot be accurately characterized as a "sale" by the pipeline to itself.

Additionally, in this case there exists more than 40 years of pipeline regulation underlying enactment of the NGPA. The lower court's interpretation of Section 2(21) brings that history to an end, without an express command from Congress. Such a long history of pipeline price regulation should not be lightly ended, by judicial creation of a fictional transaction. A long history of *lack* of regulation was the basis for this Court's declining to construe a statute to permit such regulation in *American Trucking Assoc., supra.* There is no good reason not to apply the same rationale to this case, finding that a long history of regulation is an important determinant for continuing regulation of pipeline production, when Congress gives no express command to end it.

This Court has also said, "[i]t is commonplace that courts will further legislative goals by filling the interstitial silences within a statute or regulation." But where it appears Congressional silence is not "the result of lack of prescience", but rather is the result of "betoken permission or, perhaps considered abstention", courts are not "accredited to supercede Congress or the appropriate agency." In such a case "caution must temper judicial creativity in the face of legislative or regulatory silence." *Ford Motor Credit Co.* v. *Milhollin*, 444 U.S. 555, 565 (1980). In this case Congressional silence on the subject of pipeline production "in the face of an administrative policy" for treatment of pipeline production suggests acquiescence to that policy. *Haig* v. *Agee*, 453 U.S. 280, 300 (1981).

Although Congress was silent on the definition of "first sale", it was not silent in defining the term "sale" under the NGPA. Furthermore, other sections of the NGPA support the FERC's conclusion that pipeline production was intended to be dealt with by rule. Section 203(b) provides:

> "For purposes of this section, in the case of any natural gas produced by any interstate pipeline . . . the first sale

> acquisition cost of such gas shall be determined in accordance with rules prescribed by the Commission." 15 U.S.C. §3343.

Section 501(a) provides similar guidance:

> "In general. — Except where expressly provided otherwise, the Commission shall administer this Act . . . and . . . prescribe rules and orders as it may find necessary to carry out its functions under this Act." 15 U.S.C. §3411.

Section 501 delegates to the FERC exclusive authority to administer the NGPA and to define the terms used in that act.

The Conference Report to H.R. 5289 (which became the NGPA) states that Congress provided the FERC with "authority to refine definitions of terms provided in the Act in a manner that is consistent with the definitions provided."[6] On Section 501[7], the Conference Report also provides:

> "The Commission may define terms . . . . For instance the Commission may define terms such as 'transfer for value' used in the definition of first sale; *it may also establish rules applicable to intracorporate transactions* under the first sale definition." H.R. Rep. No. 95-1752, 95th Cong., 2d Sess., p. 116, reprinted in 1978 U.S. Code Cong. & Ad. News 8800, 9033. (Emphasis Supplied)

The lower court erroneously concluded that use of the word "under" in the citation from the Conference Report immediately above "assumes that intracorporate transactions will fall within the first sale definition." 664 F.2d 530, 537.

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[6]

H.R. Rep. No. 95-1752, 96th Cong., 2d Sess. p. 69, *reprinted* in 1978 U.S. Code Cong. & Admin. News 8983, 8985.

[7]

15 U.S.C. §3411.

Because the word "under" is used after the term "transfer for value", which is itself used only in the Section 2(20) definition of "sale", the Conference Report description of authority granted the FERC to define terms must logically and gramatically relate to a "transfer for value." Use of the term "first sale" at the end of the same sentence of the Conference Report merely recognizes that Section 2(20), defining "sale", is the premise for Section 2(21), defining "first sale". Therefore, no particular significance should be attached to the word "under" in the Conference Report, and it is reasonable to conclude that the FERC has authority to regulate intracorporate transactions, pursuant to its authority to define "transfer for value."

Such an interpretation is logical because intracorporate transactions are clearly not arms-length and do not transfer anything of value. Hence, they were left to the FERC to define and regulate under the NGA, as the Conference Report expressly indicates. When an agency is expressly given such substantive authority, as the FERC was in §§ 203(b) and 501(a) of the NGPA, the agency's determination is given "legislative effect." *Schweiker* v. *Gray Panthers*, 453 U.S. 34; 69 L.Ed. 2d 460; 101 S.Ct. 2633 (1981); *Herweg* v. *Ray*, ...U.S.....; 71 L.Ed.2d 137; 102 S.Ct. .... (1982).

Congressional delegation to an agency of the power to prescribe standards entrusts to the agency, "rather than to the courts, the primary responsibility for interpreting the statutory term." Upon review, a court "is not free to set aside those regulations simply because it would have interpreted the statute in a different manner." *Batterton* v. *Francis*, 432 U.S. 416, 425 (1977). Similarly, "'reliance on legislative history is . . . a step to be taken cautiously,'" because courts "'must be wary against interpolating [their] notions of policy in the interstices of legislative provisions.'" *Piper* v. *Chris-Craft Industries, Inc.*, 430 U.S. 1, 26 (1977). In *Piper*, this Court

refused to find a fictional, implied cause of action, because the legislative history was sparse and inconclusive on the provision in question, just as it is here on the definition of "first sale" in Section 2(21). The Fifth Circuit should not have created a judicial fiction in this case either, for the same reasons.

It is unnecessary to treat intracorporate transfers (commingling) like first sales, as the lower court held it must to give meaning to the final clause of Section 2(21). That clause specifies pipeline sales of their own production will *not* be treated as first sales "unless such sale is attributable to volumes of natural gas produced by such interstate pipeline." The FERC interpreted this clause to apply only to sales at the wellhead. This interpretation did not make the "unless" clause meaningless as the Fifth Circuit opinion stated. In fact, many such wellhead sales are made to other pipelines and end users, even though most pipeline production becomes a part of the pipeline's overall gas supply for subsequent resale. However, the court's construction of the "unless" clause of Section 2(21)(B) has the rather bizarre effect of pipeline production receiving maximum ceiling prices, while independent producers' rates for similar sales are limited to the price terms of the specific contract governing the sale, by Section 101(b)(9) of the NGPA, 15 U.S.C. §3311(b)(9).

This ruling leads to a pipeline's production, not under contract, receiving higher rates than gas covered by contracts with independent producers. No court, with the protection of consumer interests in mind, can countenance this construction of the NGPA. In fact the Conference Report states "maximum lawful prices are ceiling prices only. In no case may a seller receive a higher price than his contract permits." H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 74 (1968). Thus, the decision being reviewed by this Court permits pipeline producers greater rights than the independents, by virtue of

the intracorporate transfer theory. Pipelines now qualify for full NGPA prices on their production, even though ungoverned by contract or accompanied by other indicia of a "sale".

Additionally, section 601(b)(1)(E) provides safeguards for transactions between a pipeline and its affiliates. The absence of any safeguard for intracorporate transfers demonstrates Congress did not intend they would be afforded "first sale" status. Nevertheless, the court below interpreted the statute in such a fashion that a pipeline which produces gas through an affiliate is subject to the §601(b)(1)(E) limitations, but a pipeline which does business as a single corporate entity may charge itself higher prices than it could pay an affiliate. Pipelines have no incentive to bargain for their own production, unlike the situation they face with independent producers. The higher the price, the higher the profitability.

This is just the type of indiscriminate application of the NGPA's pricing provisions that the Fifth Circuit recently rebuked. *Columbia Gas Development Corp.* v. *Federal Energy Regulatory Commission*, 651 F.2d 1146 (1981). Where, as here, a pipeline recovers on a cost-of-service basis all prudently incurred costs and also earns a reasonable return on its investment, it has already received substantial pricing incentives. To provide the pipeline with more results in injustified windfalls at the expense of consumers.

IV.

The Decision Below Results In Inequitable Windfalls To The Pipelines

It is axiomatic that courts will not construe statutes in a manner that would lead to an abuse or unjust result. *ECEE, Inc.* v. *Federal Energy Regulatory Commission*, 611 F.2d 554

(5th Cir., 1980). Yet, that is the only tangible result of the reversal of Order No. 58. The Commission pointed out (Pet. App. B-26 to B-27) that:

> "[p]ipelines receiving such treatment have enjoyed the advantage of passing on to their customers the risks of the pipeline's production ventures. Pipelines have passed on the costs of acquiring leases and the costs of exploration and development, including dry hole costs and other costs associated with unsuccessful and marginally successful ventures, in exchange for assuring their customers the opportunity to enjoy the additional volumes resulting from successful ventures at a price determined on a cost-of-service basis. The Commission therefore will not extend pricing parity to pipeline production which prior to the enactment of the NGPA was valued on a cost-of-service basis rather than by reference to area or nationwide [rates]."

Where pipelines received parity of treatment with independent producers and accepted the risks inherent in area ratemaking prior to passage of the NGPA, the FERC provided parity in pricing under Order No. 98 as an exercise of discretion under the NGA. That order prevents pipelines from making their production at NGPA prices only for two categories of gas: (1) old production from wells drilled before January 1, 1973 on leases acquired before October 7, 1969, which has always received cost-of-service treatment (i.e. gas whose development, including the cost of unsuccessful wells, was funded directly by ratepayers); and (2) production that would otherwise have been priced at area rates under Opinion No. 568 *had the pipelines themselves* not asked for and been granted direct ratepayer support when it was beneficial for them to do so.

Michigan Wisconsin Pipeline Company (MW) provides but a small example of the kind of windfall that will occur. In 1973, MW first applied to the Federal Power Commission, the FERC's predecessor, for cost of service treatment to assist its exploration and development program on leases acquired after October 7, 1969. Between 1973 and 1977, MW's customers agreed to finance these efforts in a series of Commission-approved settlements; as a result, MW received far more revenue for its production efforts than it would have received had it valued its gas at the area rates applicable to independent producers. However, in an order issuued in 1977,[8] the Commission indicated that it would not continue to approve cost of service treatment in settlement agreements unless MW made the showing of special circumstances required by Opinion No. 568.[9] MW declined this invitation in its 1977 general rate case, and began imputing to its company-owned production the equivalent area or national rate allowed independent producers.

In its first general rate case following passage of the NGPA, FERC Docket RP79-39, MW claimed the right to price its own production at the ceiling prices for "first sales." During the pendency of that proceeding, the Commission ruled in Order No. 58 that the definition of "first sale" in section 2(21) does not include sales of pipeline production which is commingled with other sources of supply. At the same time, the Commission also instituted a rulemaking in which it proposed, as an exercise of its jurisdiction under the Natural Gas Act, to con-

---

[8]

Order Modifying Initial Decision On Issues Of Advance Payments, Rate Treatment For Pipeline Production and Rate Design, *Michigan Wisconsin Pipe Line Co.*, Docket RP73-102, 42 Fed. Reg. 36,020 (July 13, 1977).

[9]

Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738 (1969), aff'd *sub nom., Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972).

tinue parity of treatment for pipeline production activities that had not been included in the pipeline's cost of service.[10] The proposed rule, however, did not appear to govern the rate treatment for MW's production, which had previously received substantial ratepayer support and guarantees through cost of service treatment, but which later had been valued at area rates.[11] In order to finalize a rate treatment for MW's production without further FERC proceedings, the parties to RP79-39, including Michigan, negotiated an agreement under which MW would henceforth be permitted to value its own production at NGPA prices. In exchange, MW agreed to refund to its customers $7.44 million, the amount by which cost of service treatment between 1973 and 1977 exceeded the amount MW would have collected if it had been forced to price its own production at area rates. The agreement also provides that MW will recoup the $7.44 million if this Court holds that all pipeline production qualifies for first sale treatment regardless of whether that production has been afforded cost of service treatment.

The Fifth Circuit's decision upset this arrangement without providing MW any new incentives. MW will merely keep the $7.44 million, which represents a direct subsidy by ratepayers.

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[10]

Notice of Proposed Rulemaking, Pricing of Pipeline and Affiliate Production Under the Natural Gas Act, Docket No. RM80-6. (R.3035-52). The proposed rules were ultimately made final with minor modification in Order No. 98, reversed in *Consolidated Gas Supply Corp. v. FERC*, No. 80-4010.

[11]

RM80-6 could have been read as requiring MW to return to cost of service treatment, for it denied NGPA-parity prices to any "natural gas produced from leases acquired before November 15, 1979, which has *ever* been granted cost of service treatment." (Emphasis Added) However, in the preamble to the proposed rule, the Commission referred specifically to the history of MW's production, and stated that "[t]his matter will be the subject of a separate order."

Michigan does not believe that Congress intended to play a cruel hoax on natural gas consumers by allowing pipelines to collect NGPA prices for gas developed at ratepayer expense and risk.

This windfall and others resulting from receipt of NGPA prices for gas produced at ratepayer expense and risk is neither equitable nor consistent with Congressional intent. Representative John D. Dingell of Michigan's 16th District, manager of the NGPA conference report in the House said, "[t]he Natural Gas Policy Act provides reasonable price incentives, while avoiding windfall profits" 124 Cong. Rec., Oct 14, 1978, H 13115. Of the NGPA ceiling prices, Representative Dingell stated:

> "A key aspect of the conference report is the focusing of price increases on categories of production which promise the greatest supply response at the lowest cost to consumers. The deregulation provisions provide the incentive required for producers to undertake investments in production projects. . . ." 124 Cong. Rec., Oct 14, 1978, H 13114.

The benefit of NGPA prices was clearly intended to follow the burden of investment in a risky business, i.e., exploration and development of natural gas supplies. But the decision of the Court below rewards pipelines even though they took no risk under cost-of-service pricing. The risk was actually placed upon the consumer, but he is denied the benefits of the investment.

When over 40 years of pipeline regulation under the NGA is considered in conjunction with the definition of "sale" in Section 2(20), the legislative history related to that section, other provisions of the NGPA, and the rules of statutory construction cited herein, it becomes readily apparent that the

court below should not have resorted in this case to the judicial fiction of imputing a sale at the wellhead from a factually fictional intracorporate transaction. On the contrary, there is good reason to conclude, from the long history of differing regulatory treatment of pipelines and independent producers which relieved pipelines of the risks of production, that Congress intended to exclude pipeline production from the NGPA and leave it to FERC regulation under the NGA.

CONCLUSION

The decision of the court below has a significant economic impact on gas consumers and an enormous effect on state regulation of natural gas production as it existed before the decision. The court below judicially created a fictional transaction completely eliminating the long history of regulation of pipeline production at the federal level, without clear indication of Congressional intent to do so. Michigan therefore urges this Court to reverse and vacate the decision and mandate of the Court below.

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Brief for the United States

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In the Supreme Court of the United States

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BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

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QUESTION PRESENTED

In Title I of the Natural Gas Policy Act of 1978 (entitled "Wellhead Pricing"), 15 U.S.C. (Supp. V) 3311 *et seq.*, Congress established a new and intricate incentive pricing scheme for the "first sale" of natural gas. Unquestionably, this scheme was meant to reach gas produced and sold at the wellhead by independent producers and pipeline producers. The question presented is whether Congress also intended to require the Federal Energy Regulatory Commission to treat as a "first sale" within this pricing scheme either an intracorporate transfer of pipeline produced gas from a pipeline's production division to its transmission division, or the eventual sale of such gas to the pipeline's regular customers after the gas has been commingled with purchased gas and transported downstream by the pipeline as part of its general system supply.

TABLE OF CONTENTS

	Page
Opinions below	2
Jurisdiction	2
Statutes involved	2
Statement:	
A. The statutory and regulatory background	3
B. The Commission's Rules	7
C. The opinion of the court of appeals	11
Introduction and summary of argument	12
Argument:	
The Commission correctly determined that under the Natural Gas Policy Act it is required to accord "first sale" treatment only to wellhead or field sales of natural gas and not to transactions involving pipeline produced gas that has been transported by the producing pipeline as part of its mixed system supply and sold downstream to its system customers	15
A. The Commission's interpretation is strongly supported by the literal language of Section 2(21)(B) of the Act	16
B. The structure and history of the NGPA fully support the Commission's view	22
C. The Commission's analysis is consistent with the policies underlying the NGPA	28
1. The Commission's approach will not perpetuate a dual market for interstate and intrastate gas or discourage increased production	28
2. The Commission properly recognized that the policies underlying the NGPA do not require that pipeline producers be treated in all instances identically to independent producers	30

Argument—Continued: Page

3. The Commission properly exercised its authority under the Natural Gas Act in permitting sales of parity priced gas to be valued at NGPA levels 36

4. Both the court's intracorporate transfer "first Sale" and respondent's downstream "first sale" would create a substantial reworking of state and federal regulatory schemes in ways Congress could not have intended 39

D. The court of appeals erred in failing to defer to the Commission's interpretation of the statute 40

Conclusion 43

Appendix 1a

TABLE OF AUTHORITIES

Cases:

American Tobacco Co. v. *Patterson*, No. 80-1199 (Apr. 5, 1982) 16

Blum v. *Bacon*, No. 81-770 (June 14, 1982) ... 40

Canadian River Gas Co., In re, 3 F.P.C. 32, aff'd *sub nom. Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 ..... 4, 5, 12

Carlton v. *United States*, 385 F.2d 238 19

Chemehuevi Tribe of Indians v. *FPC*, 420 U.S. 395 22

Columbia Gas Development Corp. v. *FERC*, 651 F.2d 1146 ..... 26, 31, 35, 36

Columbian Fuel Corp., In re, 2 F.P.C. 200 ..... 4, 5, 25, 32, 38

Consumer Product Safety Commission v. *GTE Sylvania, Inc.*, 447 U.S. 102 16

Coulter Electronics, Inc. v. *Department of Revenue*, 365 So.2d 806 19

Ecee, Inc. v. *FERC*, 645 F.2d 339 41

Cases—Continued: Page

FEC v. *Democratic Senatorial Campaign Committee*, 454 U.S. 27 ..... 40-41, 42
Gulf Oil Corp. v. *Copp Paving Co.*, 419 U.S. 186 25
Howe v. *Smith*, 452 U.S. 473 ..... 16, 42
Just and Reasonable National Rates for Sales of Natural Gas, 52 F.P.C. 1604 6
Marvin E. Boyer Co., 3 F.E.A. ¶ 83,088..... 20
Maryland v. *Louisiana*, 451 U.S. 725 22
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Pennzoil Co. v. *FERC*, 645 F.2d 360, cert. denied, No. 81-340 (Jan. 11, 1982) 31
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Public Service Electric & Gas Co. v. *FPC*, 372 F.2d 1 19
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Cases—Continued: Page

Robertson v. *Railroad Labor Board*, 268 U.S. 619 13

Southern Louisiana Area Rate Cases v. *FPC*, 428 F.2d 407 33

Sunray Mid-Continent Oil Co. v. *FPC*, 364 U.S. 137 20

Tenneco Corp., 28 F.P.C. 382 6

Udall v. *Tallman*, 380 U.S. 1 41

United Gas Co. v. *Mobile Gas Corp.*, 350 U.S. 332 19

Utah Concrete Products Corp. v. *State Tax Commission*, 101 Utah 513, 125 P.2d 408 ... 19

Watt v. *Alaska*, 451 U.S. 259 26

Wisconsin v. *FPC*, 373 U.S. 294 4

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Department of Energy Organization Act, Pub. L. No. 95-91, Section 403(d), 91 Stat. 585 ... 20

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Natural Gas Act, 15 U.S.C. (& Supp. V) 717 *et seq.* 4

15 U.S.C. 717c 35

15 U.S.C. 717c(c) 19

15 U.S.C. 717c(d) 19

15 U.S.C. (& Supp. V) 717f(c) 20

15 U.S.C. (Supp. V) 717f(c)(2)(B) 40

Natural Gas Policy Act of 1978, 15 U.S.C. (Supp. V) 3301 *et seq.* 3

Section 2(15), 15 U.S.C. (Supp. V) 3301(15) 21

Section 2(20), 15 U.S.C. (Supp. V) 3301(20) 2, 7, 18

Section 2(21), 15 U.S.C. (Supp. V) 3301(21) 2, 7, 14, 20, 21

Section 2(21)(A), 15 U.S.C. (Supp. V) 3301(21)(A) 7, 16

Statutes and regulations—Continued: Page

Section 2(21)(A)(i), 15 U.S.C. (Supp. V) 3301(21)(A)(i) 7, 9
Section 2(21)(A)(ii), 15 U.S.C. (Supp. V) 3301(21)(A)(ii) 7, 9
Section 2(21)(A)(iii), 15 U.S.C. (Supp. V) 3301(21)(A)(iii) 7, 9
Section 2(21)(A)(iv), 15 U.S.C. (Supp. V) 3301(21)(A)(iv) 9
Section 2(21)(A)(v), 15 U.S.C. (Supp. V) 3301(21)(A)(v) 9, 27, 28
Section 2(21)(B), 15 U.S.C. (Supp. V) 3301(21)(B)..... passim
Section 2(26), 15 U.S.C. (Supp. V) 3301(26) 21
Section 2(27), 15 U.S.C. (Supp. V), 3301(27) 21
Section 101(a), 15 U.S.C. (Supp. V) 3311(a) 37
Section 101(b)(9), 15 U.S.C. (Supp. V) 3311(b)(9) 31
Section 102, 15 U.S.C. (Supp. V) 3312 6
Section 102(b), 15 U.S.C. (Supp. V) 3312(b) 34
Section 103, 15 U.S.C. (Supp. V) 3313 6
Section 103(b), 15 U.S.C. (Supp. V) 3313(b) 34
Section 104, 15 U.S.C. (Supp. V) 3314 ..... 6, 31-32, 37
Section 104(b)(1)(A), 15 U.S.C. (Supp. V) 3314(b)(1)(A) 37
Section 105, 15 U.S.C. (Supp. V) 3315 7
Section 106, 15 U.S.C. (Supp. V) 3316 7
Section 107, 15 U.S.C. (Supp. V) 3317 7
Section 108, 15 U.S.C. (Supp. V) 3318 ..... 7, 34, 35, 37
Section 108(a), 15 U.S.C. (Supp. V) 3318(a) 34
Section 109, 15 U.S.C. (Supp. V) 3319 7

Statutes and regulations—Continued: Page

Section 110(a), 15 U.S.C. (Supp. V) 3320(a) 40
Section 110(a)(1), 15 U.S.C. (Supp. V) 3320(a)(1) 17
Section 121, 15 U.S.C. (Supp. V) 3331 7
Section 203, 15 U.S.C. (Supp. V) 3343 26
Section 203(b), 15 U.S.C. (Supp. V) 3343(b) 27
Section 203(b)(1), 15 U.S.C. (Supp. V) 3343(b)(1) 26
Section 203(b)(2), 15 U.S.C. (Supp. V) 3343(b)(2) 27
Section 303(d), 15 U.S.C. (Supp. V) 3363(d) 40
Section 501(a), 15 U.S.C. (Supp. V) 3411(a) 9
Section 503(e)(2)(B), 15 U.S.C. (Supp. V) 3413(e)(2)(B) 18
Section 601, 15 U.S.C. (Supp. V) 3431 .... 13, 22
Section 601(a), 15 U.S.C. (Supp. V) 3431(a) 40
Section 601(b)(1)(E), 15 U.S.C. (Supp. V) 3431(b)(1)(E) 23
Section 602(a), 15 U.S.C. (Supp. V) 3432(a) 31

18 C.F.R.:
Section 2.56a(a)(1) 37
Section 2.56a(a)(2) 37
Section 154.38 38
Section 154.38(d)(4) 38
Section 271.101 35
Section 270.203(a) 30

Miscellaneous:
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Black's Law Dictionary (5th ed. 1979) 19
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Miscellaneous—Continued: Page

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pp. 38360-38361 31
p. 38362 24
p. 38364 37
p. 38367 27
pp. 38374-38375 42

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2A Sutherland Statutory Construction (C. Sands rev. 1973) 22

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BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A-1 to A-15)[1] is reported at 664 F.2d 530. The orders of the Federal Energy Regulatory Commission (Pet. App. B-1 to B-13, B-14 to B-49 and B-50 to B-82) are not reported.

JURISDICTION

The judgments of the court of appeals (Pet. App. C-1; 82-19 Pet. App. 1a-2a) were entered on December 23, 1981. Timely petitions for rehearing were denied on February 5, 1982 (Pet. App. C-3 to C-4). The petitions for a writ of certiorari were filed on April 12, 1982, in No. 81-1889; on April 23, 1982, in No. 81-1958; and on May 3, 1982, in No. 81-2042. Justice White extended the time for filing the petition in No. 82-19 to and including July 5, 1982 (a holiday), and that petition was filed on July 6, 1982. The petitions were all granted on October 4, 1982. The jurisdiction of this Court rests on 28 U.S.C. 1254(1) and 15 U.S.C. (Supp. V) 3416(a)(4).

STATUTES INVOLVED

1. Section 2(20) of the Natural Gas Policy Act of 1978, 15 U.S.C. (Supp. V) 3301(20), provides:

> The term "sale" means any sale, exchange, or other transfer for value.

2. Section 2(21) of the Natural Gas Policy Act of 1978, 15 U.S.C. (Supp. V) 3301(21) provides:

> (A) General rule
>
> The term "first sale" means any sale of any volume of natural gas—
>
> (i) to any interstate pipeline or intrastate pipeline;
>
> (ii) to any local distribution company;
>
> (iii) to any person for use by such person;

---

[1] "Pet. App." refers to the appendix to the petition for a writ of certiorari in No. 81-1889.

(iv) which precedes any sale described in clauses (i), (ii), or (iii); and

(v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this chapter.

(B) Certain sales not included

Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

STATEMENT

A. The Statutory and Regulatory Background

1. Most of the nation's natural gas supply is produced by independent producers who typically sell their output at the wellhead or elsewhere in the field[2] to interstate and intrastate pipeline companies, which, in turn, transport the gas and resell it downstream to their regular system customers. A portion of the nation's gas supply, however, is produced by the pipelines themselves.[3] Generally, this gas is commingled with the gas purchased from independent producers and is sold downstream as part of the pipeline's general system supply.

Prior to the passage of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. (Supp. V) 3301 *et seq.*, the Com-

[2] Sales in the gas field take place either at the wellhead or at a point along the gathering line.

[3] There is little compiled data available on the amount of gas produced by intrastate pipelines. With respect to interstate pipelines, the available data show that as of the end of calendar year 1981, interstate pipelines collectively owned 13.7 Tcf (trillion cubic feet) of natural gas reserves, which represent 13.9% of total United States reserves. Of gas actually produced in 1981, interstate pipelines were responsible for 5.3% of the total. *Energy Data Report, Domestic Natural Gas Reserves and Production Dedicated To Interstate Pipeline Companies, 1981*, at 2 (U.S. Dept. of Energy, July 27, 1982).

mission[4] regulated the price of all gas transported and sold in interstate commerce under the Natural Gas Act, 15 U.S.C. (& Supp. V) 717 *et seq.* Pursuant to the Commission's authority under that Act, it developed discrete pricing schemes for gas produced by independent producers and for gas produced by pipelines.[5] The Commission's regulatory approach with regard to independent producers focused on establishing uniform rates and on providing sufficient incentives to encourage producers to dedicate greater volumes of gas to the interstate market.[6]

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[4] The Federal Power Commission was the predecessor of the Federal Energy Regulatory Commission. Both are referred to herein as the "Commission."

[5] This difference has historical roots. Until this Court decided, in *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954), that the Commission had jurisdiction under the Natural Gas Act to regulate wellhead sales by independent producers, the Commission was of the view that its regulatory authority extended only to the sale and transportation of natural gas by pipelines in interstate commerce. *In re Columbian Fuel Corp.*, 2 F.P.C. 200, 206 (1940); *In re Canadian River Gas Co.*, 3 F.P.C. 32, 40 (1942), aff'd *sub nom. Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945). See *Permian Basin Area Rate Cases*, 390 U.S. 747, 756 n.7 (1968).

[6] This approach ultimately took the form of a pricing methodology that utilized a representative average cost of all producers in a particular area, rather than focusing on the individual costs of each entity subject to regulation. See *Wisconsin* v. *FPC*, 373 U.S. 294, 298-299 (1963). By this method, the Commission sought to "employ price functionally, as a tool to encourage discovery and production of appropriate supplies of natural gas." *Permian Basin Area Rate Cases*, *supra*, 390 U.S. at 760. The area rates, and the subsequently adopted national rates, specified separate, fixed components for "Successful Well Costs" and "Dry Hole Costs," so that a producer potentially could recover both types of costs from his sales of flowing gas. See *National Rates For Jurisdictional Sales of Natural Gas*, 56 F.P.C. 509, 543-544 (1976), aff'd *sub nom. American Public Gas Association* v. *FPC*, 567 F.2d 1016 (D.C. Cir. 1977), cert. denied, 435 U.S. 907 (1978). An incentive was thereby provided: those independent producers that operated below the average cost levels on which the area or nationwide rates were based, or that enjoyed a higher success rate in well completion, earned a greater return while those that operated at higher than average costs or encountered more dry holes earned less. In either case, however, the producers' costs could only be recovered through actual sales.

On the other hand, the Commission, as early as 1942, treated pipeline production as an integral part of the pipeline's transmission business and regulated both production and transmission on a cost of service basis. *In re Canadian River Gas Co.*, 3 F.P.C. 32, 40 (1942), aff'd *sub nom. Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945).[7] Under this methodology, a pipeline was permitted to recover only its actual costs of production including a reasonable return on investment.[8] Over time, the Commission came to allow certain categories of pipeline production to be priced on a parity with independently produced gas (under area and national rates), but retained others on a cost of service basis.[9]

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[7] This approach was presaged in the Commission's jurisdictional decision in *In re Columbian Fuel Corp.*, *supra*, where the Commission differentiated between pipeline production and independent producer production. Its view was that "[w]here a big transporting company owned its own wells and gathering lines, there would be but one wholesale * * * transaction to bring under Federal regulation and all provisions of the Act involving production and gathering would apply." 2 F.P.C. at 206.

[8] Under the cost of service approach, a pipeline computes the amount of revenues needed, on a test year basis, to cover its exploration costs, including the return sought on production investment (i.e., rate base); this amount is then added to the revenue requirements for the pipeline's wholesale rates. See Pet. App. B-21. The net effect is to shift all risks to the consumers since pipeline producers are permitted to recover all prudently incurred costs, relating not only to successful drilling activities, but also to "dry hole costs and other costs associated with unsuccessful and marginally successful ventures * * *" (*id.* at B-27).

[9] As initially formulated in 1969 and refined in 1972, the Commission's regulatory scheme with regard to pipeline production was as follows:

(1)When a pipeline producer functioned like an independent producer by selling its production directly in the field (a "field" or "wellhead" sale), usually to another pipeline, the Commission accorded those "off-system" sales independent producer pricing. As was the case with wellhead sales by independent producers, each off-system pipeline sale was made pursuant to a specific contract and, if a sale for resale in interstate commerce, pursuant to a certificate of public convenience and necessity issued by the Commission. In addition, the pipeline was required to file with the Commission a producer rate schedule covering

2. By the late 1960's, however, in the face of a rapidly increasing demand for natural gas, there emerged a sharp division between the regulated interstate market, on the one hand, and the intrastate markets, which had not been subject to Commission regulation under the Natural Gas Act. By the 1970's, this artificial division had solidified and the nation's gas situation worsened. The prices for gas in the intrastate markets were substantially higher than in the interstate market; this price disparity adversely affected the dedication of gas to the interstate market, resulting in serious shortages of gas available for interstate sale. A central purpose of Congress in enacting the NGPA was to eliminate these dual markets and create a single national market where both interstate and intrastate purchasers would have equal access to new gas supplies without substantial price disparity. In addition, Congress sought to encourage the production of new gas through an incentive pricing scheme.

Title I of the NGPA, entitled "Wellhead Pricing," serves both of these objectives by establishing an intricate system of pricing schedules for the "first sale" of natural gas.[10] Sec-

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the transaction, as would an independent producer in similar circumstances. See, e.g., *Tenneco Corp.*, 28 F.P.C. 382 (1962) (listing numerous field sale contracts, certificates and rate schedules covering sales by producing affiliates to parent transmission company).

(2)Pipeline production arising from post-October 7, 1969 leases or from wells commenced after January 1, 1973 (regardless of lease date) that was transported and sold through a pipeline's own transmission system (i.e., from mixed system supply) received independent producer pricing, absent a showing of "special circumstances" warranting cost of service treatment. See *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738, 745 (1969), aff'd *sub nom. City of Chicago* v. *FPC*, 458 F.2d 731 (D.C. Cir. 1971), cert. denied, 405 U.S. 1074 (1972); *Just and Reasonable National Rates for Sales of Natural Gas*, 52 F.P.C. 1604, 1634 (1974).

(3)All other pipeline production was continued on traditional cost of service methodology.

[10] Section 102 (15 U.S.C. (Supp. V) 3312) prescribes the maximum lawful price for first sales of "new" natural gas and certain gas produced from the Outer Continental Shelf; Section 103 (15 U.S.C. (Supp. V) 3313) prescribes the maximum lawful price for first sales of gas produced from new onshore production wells; Section 104 (15 U.S.C. (Supp. V) 3314) imposes ceiling prices for first sales of gas that was flowing in interstate commerce at the time of enactment of the NGPA,

tion 2(21)(A) of the Act, 15 U.S.C. (Supp. V) 3301 (21)(A), defines "first sale" generally as "any sale of any volume of natural gas" to a specified purchaser, including an interstate pipeline, an intrastate pipeline, a local distribution company or an end user. However, Section 2(21)(B) provides that a "first sale"

> * * * shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

15 U.S.C. (Supp. V) 3301(21)(B). The Act defines "sale" as "any sale, exchange, or other transfer for value." Section 2(20), 15 U.S.C. (Supp. V) 3301(20).

B. The Commission's Rules

In a rulemaking commenced pursuant to the NGPA,[11] the Commission interpreted the NGPA as having supplanted completely the incentive pricing system that the Commission had devised under the Natural Gas Act for gas produced by independent producers. It found that a sale of gas produced by independent producers falls within the statutory definition of "first sale"[12] and thus is governed by the pricing scheme established in Title I. It determined fur-

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November 1978; Section 105 (15 U.S.C. (Supp. V) 3315) covers first sales of natural gas flowing in intrastate commerce as of November 1978; Section 106 (15 U.S.C. (Supp. V) 3316) establishes ceiling prices for both interstate and intrastate sales under "rollover" contracts; Section 107 (15 U.S.C. (Supp. V) 3317) prescribes the maximum lawful price for first sales of high-cost gas; Section 108 (15 U.S.C. (Supp. V) 3318) prescribes the maximum lawful price for "stripper well" natural gas; and Section 109 (15 U.S.C. (Supp. V) 3319) establishes the first sale price for gas not covered by any of the foregoing categories. Section 121 (15 U.S.C. (Supp. V) 3331) establishes a schedule for deregulation of several of these categories of gas.

[11] Order No. 58 (Pet. App. B-1 to B-13), affirmed on rehearing in Order No. 102 (Pet. App. B-50 to B-82).

[12] I.e., as "any sale of any volume of natural gas" to a specified purchaser, including an interstate pipeline, an intrastate pipeline, a local distribution company or an end user. 15 U.S.C. (Supp. V) 3301(21)(A)(i), (ii), and (iii).

ther that a wellhead or field sale by a pipeline also qualifies as a "first sale" under the NGPA (Pet. App. B-2). In the Commission's view (*id.* at B-53), "[w]ellhead or field sales [by pipelines] clearly are sales attributable to a pipeline's * * * own production," since the gas is sold in the producing field in discrete blocks and not as part of the pipeline's general system supply.

The Commission found, however, that a downstream sale by a pipeline to its system customers from its mixed system supply, which is comprised of volumes of gas purchased from independent producers commingled with gas produced by the pipeline itself, does not constitute a "first sale" under the Act. The Commission concluded that for a sale to be "attributable" in the statutory sense to a pipeline's own production, the sale would have to be "comprised exclusively" of that production (Pet. App. B-2, B-12). The Commission (*id.* at B-61) rejected the argument that "section 2(21)(B) guarantees a pipeline the right to collect a first sale price for all volumes of natural gas produced by that pipeline or distributor without regard to the type of transaction or the manner in which the gas is transferred." The Commission reasoned (*id.* at B-61 to B-62):

> Section 2(21)(B) speaks in terms of sales, not volumes of natural gas, and excludes a pipeline or distributor sale from first sale treatment "unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline or local distribution company, or any affiliate thereof."

The Commission stressed that if the NGPA were read to apply to routine intrastate pipeline or local distribution company sales from mixed system supply, federal regulation would displace the retail ratemaking jurisdiction of state and local authorities over such mixed volume sales, an intrusion into the local retail markets that was not intended by Congress in enacting the NGPA (*id.* at B-4, B-62).

The Commission also rejected the contention made by some pipelines that the term "attributable" as used in the statute means "imputable," and that the statute thus requires the Commission to impute a "first sale" at the wellhead to an intracorporate transfer of gas from a pipeline's

producing division to its transmission division. While the Commission was of the view that under its authority to prevent circumvention of the Act[13] it has the power to define an intracorporate transfer as a "first sale," it concluded that such a determination was neither appropriate nor necessary (Pet. App. B-65 to B-66). It emphasized that such transfers had not been considered sales under the Natural Gas Act inasmuch as there were no contracts or certificates applicable to such hypothetical transactions. Nor did it find anything in the NGPA that compelled it to regard as a sale "an event that is recorded solely on the books and records of the pipeline and that occurs without *** contract, bargaining, or certification" (*id.* at B-66).

Thus, as a matter of statutory interpretation, the Commission concluded that the only sales involving pipeline produced gas that necessarily are entitled to "first sale" status under the NGPA are wellhead or field sales by a pipeline of its own production.

2. In a separate rulemaking under the Natural Gas Act,[14] the Commission enunciated its policy with respect to pipeline production that is not sold at the wellhead or in the field but is commingled with purchased gas as part of the pipeline's system supply. It found that "Congress left to the Commission the task of harmonizing its statutory mandate

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[13] Section 2(21)(A)(v), 15 U.S.C. (Supp. V) 3301(21)(A)(v), gives the Commission the authority to define as a "first sale" any sale of any volume of natural gas which precedes or follows any sale described in Section 2(21)(A)(i) through (iv), 15 U.S.C (Supp. V) 3301(21)(A)(i) through (iv), in order to prevent circumvention of any maximum lawful price established under the NGPA. In addition, Section 501(a), 15 U.S.C. (Supp. V) 3411(a), gives the Commission broad rulemaking authority to carry out the purposes of the NGPA. The Conference Report explains that "[t]he authority to prescribe rules and orders necessary to carry out the provisions of this Act includes the authority to issue rules and orders necessary to prevent circumvention of the Act." H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 116 (1978). To this end, the "Commission may define terms such as 'transfer for value' used in the definition of first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition." *Ibid.*

[14] Order No. 98 (Pet. App. B-14 to B-49), affirmed on rehearing in Order No. 102 (Pet. App. B-50 to B-82).

to implement the NGPA pricing scheme with its continuing authority under the [Natural Gas Act] to determine the price treatment of natural gas produced by interstate pipelines and sold in mixed volume sales" (Pet. App. B-24; see also *id.* at B-18).

In the Commission's view, the arguments in favor of a policy of pricing parity among independent and pipeline producers—a policy that the Commission had initiated in 1969 and refined in 1972 (see note 9, *supra*)—had become even "more compelling" with the enactment of the NGPA (Pet. App. B-24). The Commission recognized that "[i]f pipeline producers were held to pre-NGPA prices, or were subject to a newly established cost-based nationwide rate, they would in many instances be unable to compete with independent producers in acquiring new leases. The resulting disincentive to pipeline production would deny the pipeline customers a more certain stream of additional supplies" (*id.* at B-25). Accordingly, the Commission determined that "the valuation of pipeline production by reference to NGPA rates represents the most reasonable reconciliation of consumer and producer interests and therefore achieves a just and reasonable result" (*id.* at B-31; footnote omitted).[15]

The Commission concluded, however, that a similar approach was not warranted as to pipeline production that had been receiving cost of service treatment. As the Commission pointed out (Pet. App. B-26 to B-27):

> Pipelines receiving such treatment have enjoyed the advantage of passing on to their customers the risks of the pipeline's production ventures. Pipelines have passed on the costs of acquiring leases and the costs of exploration and development, including dry hole costs and other costs associated with unsuccessful and marginally successful ventures, in exchange for assuring their customers the opportunity to enjoy the additional volumes resulting from successful ventures at a price

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[15] In making that determination, the Commission ruled, under its Natural Gas Act authority, that "pipeline production may not be valued at a rate in excess of the amount paid in comparable sales between persons not affiliated with the interstate pipeline or with each other" (Pet. App. B-37).

> determined on a cost-of-service basis. The Commission therefore will not extend pricing parity to pipeline production which prior to the enactment of the NGPA was valued on a cost-of-service basis rather than by reference to area or nationwide [rates].

In the Commission's opinion, to "vary this policy * * * would deprive [pipeline customers] of price benefits they should receive in exchange for assuming the risk of a pipeline's production ventures" (*id.* at B-73).

C. The Opinion of the Court of Appeals

The court of appeals vacated the Commission's rules (Pet. App. A-1 to A-15). The court held that "Congress clearly intended for any production attributable to [a pipeline] * * * to be accorded first sale status under the NGPA and * * * Congress contemplated that the intracorporate transfer of pipeline production to the pipeline would be treated as the first sale" (*id.* at A-15). Thus, the court ruled that the Commission had erred in limiting "first sale" treatment solely to sales of pipeline produced gas at the wellhead and in asserting Natural Gas Act jurisdiction under its parity pricing policy to pipeline production that, the court believed, was automatically entitled to NGPA prices under the "first sale" definition in the NGPA. The court refused to defer to the Commission on these matters, reasoning that the Commission's approach was not based on a longstanding interpretation and was not in an area of agency expertise, and, while it was a contemporaneous interpretation of a new statute, the Commission had "had no input into the development of the term 'first sale'" (*id.* at A-7).

Under the court's analysis, the first clause of Section 2(21)(B) was meant to deny "first sale" status to downstream sales of gas to a pipeline's customers (Pet. App. A-8).[16] The court believed that the "unless" clause of Sec-

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[16] To this extent, the court agreed with the Commission's determination that the language of Section 2(21)(B) precludes giving "first sale" treatment to a sale from a pipeline's mixed system supply to a regular customer even though that sale may include pipeline produced gas, since it also contains gas purchased from independent producers that already has received "first sale" treatment (Pet. App. A-8).

tion 2(21)(B) could only have meaning if it is interpreted "as granting 'first sale' status to gas which is attributable to pipeline production" (Pet. App. A-9). Under the court's interpretation, "the intracorporate transfer from the production division of the pipeline to the transportation division of the pipeline would constitute the first sale" (*id.* at A-11).[17] Otherwise, the court thought, all pipeline produced gas would be excluded from NGPA pricing (*id.* at A-8 to A-9), thus "creating a distinction between pipeline and independent producers" (*id.* at A-9) that the court believed was not supported by the purposes underlying enactment of the NGPA.

The court summarily disposed of the Commission's approach with respect to cost of service gas, noting that the Commission's cost of service decisions constituted "exceptions to the application of area or national rates [and] represent historical practices the effect of which is continually diminished as early wells cease producing gas. They do not affect our decision" (Pet. App. A-3 n.1). As for the Commission's rule under the Natural Gas Act applying NGPA prices to pipeline production that was subject to the parity pricing policy, the court characterized this approach as "sophistic" and "in no way justif[ying] departure from the congressional purpose in the first instance" (*id.* at A-9).

INTRODUCTION AND SUMMARY OF ARGUMENT

Some forty years ago, shortly after the inception of pipeline regulation under the Natural Gas Act, the Commission concluded that a pipeline's production and gathering operations were an integral part of its total operations, and, accordingly, it determined that the costs of such operations had to be taken into account in regulating the pipeline's rates and charges for the sale and transportation of gas in interstate commerce. *In re Canadian River Gas Co.*, 3 F.P.C. 32, 40 (1942), aff'd *sub nom. Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945). The broad question

[17] The court noted that the Commission had refused to treat an intracorporate transfer as a "first sale" based on its view that no "sale" takes place in such a situation (Pet. App. A-14).

at issue here is the extent to which Congress, in enacting the NGPA, meant to modify that regulatory scheme as regards pipeline production.

The decision below would completely eradicate this historical regulatory framework, and supplant it with NGPA pricing. But in Section 601 of the NGPA, 15 U.S.C. (Supp. V) 3431, Congress specifically delineated those areas in which the Commission's traditional Natural Gas Act authority is to be modified, and otherwise left it to the Commission, in the exercise of its discretion, to harmonize implementation of the NGPA with the existing scheme of regulation under the Natural Gas Act. Nowhere in these limitations did Congress address the Commission's treatment of pipeline production. In these circumstances, "[i]t is not lightly to be assumed that Congress intended to depart from a long established policy." *Robertson* v. *Railroad Labor Board*, 268 U.S. 619, 627 (1925). The central thrust of our argument is that if, as the court of appeals assumed, Congress meant to effect a complete overhaul of the Commission's role in regulating pipeline production, it would have expressed that intent in a more direct fashion.

Congress had two basic purposes in enacting the Natural Gas Policy Act: (1) to eliminate the dual market for gas, and (2) to encourage increased gas production. Those purposes are clearly served by recognizing that independent producers are eligible for the pricing benefits of Title I. Application of the NGPA's incentive pricing provisions to the production and sale activities of independent producers has a direct impact in eliminating the disparities spawned by the bifurcated market problem. That goal is also served by granting "first sale" status to a pipeline's sale at the wellhead or in the field, which is the functional equivalent of an independent producer sale.

There is no indication, however, that granting NGPA pricing to pipeline production across the board either would help to solve the dual market problem or is necessary to spur production of all categories of gas. In the main, application of NGPA prices to all pipeline production would do nothing but allow pipelines to revalue cost of service gas at higher levels and thus reap an unjustified windfall.

The court of appeals, however, concluded that Congress intended NGPA prices to be applicable to all pipeline produced gas, and it construed the NGPA as requiring that a transfer of pipeline produced gas from a pipeline's production division to its transmission division (i.e., an "intracorporate transfer") be treated a "first sale." Several respondents present the alternative argument, rejected by the court below, that pipeline production is entitled to "first sale" treatment after it has been commingled with gas purchased from other sources and transported and sold downstream to the pipeline's regular customers as part of the pipeline's general system supply.

The court of appeals erred in rejecting the Commission's view that, with respect to pipeline produced gas, only a sale comprised exclusively of pipeline production—e.g., a wellhead sale—constitutes a "first sale" and thus automatically qualifies for the incentive prices of the Act. The Commission's interpretation is consistent, not only with the policies of the NGPA discussed above, but also with the language, structure and history of the Act. Accordingly, the court below should have deferred to the reasonable construction by the agency charged with administering and enforcing the statute.

Section 2(21) of the NGPA establishes the general rule that a pipeline's sale of its own production is not a "first sale." The statutory language clearly indicates that, in order to constitute a "first sale," a sale of gas by a pipeline must be "attributable" in its entirety to the pipeline's own production. A sale by a pipeline from its mixed system supply far downstream from the wellhead cannot be "attributable" to the pipeline's own production, because such a sale is comprised of gas from various sources. Moreover, an intracorporate transfer of gas also cannot constitute a "first sale" because it is not a "sale" as that term is defined in Section 2(20) of the Act. An intracorporate transfer, which merely reflects the entries in a pipeline's books and records, has none of the traditional indicia of a sale, such as a transfer of title or an exchange of consideration.

The structure of the NGPA links the concept of "first sale" with "wellhead prices," which suggests that downstream

sales do not qualify for the incentive pricing benefits of the Act. Other provisions of the NGPA indicate that Congress did not intend that an intracorporate transfer automatically qualifies for "first sale" treatment. In addition, the legislative history supports the Commission's view that "first sale" means an *actual* sale of gas *in the field*, and not a fictional transaction such as an intracorporate transfer, or a downstream sale from a pipeline's mixed system supply. Finally, adoption of either the "intracorporate transfer" theory or the "downstream sale" theory would disrupt the Act's carefully tailored regulatory structure and the delicate balance that Congress sought to preserve between federal and state regulation.

ARGUMENT

THE COMMISSION CORRECTLY DETERMINED THAT UNDER THE NATURAL GAS POLICY ACT IT IS REQUIRED TO ACCORD "FIRST SALE" TREATMENT ONLY TO WELLHEAD OR FIELD SALES OF NATURAL GAS AND NOT TO TRANSACTIONS INVOLVING PIPELINE PRODUCED GAS THAT HAS BEEN TRANSPORTED BY THE PRODUCING PIPELINE AS PART OF ITS MIXED SYSTEM SUPPLY AND SOLD DOWNSTREAM TO ITS SYSTEM CUSTOMERS

Section 2(21)(B) of the NGPA provides that a sale of natural gas by a pipeline is not a "first sale" unless the "sale is attributable to" the pipeline's own production. The Commission interpreted this statutory language to mean that only a sale comprised *exclusively* of pipeline produced gas necessarily constitutes a "first sale," thus automatically qualifying for the incentive pricing benefits of Title I. The court of appeals held, however, that *any* gas produced by a pipeline must be given "first sale" treatment under the Act, even if that gas is not actually sold by the producing pipeline until after it has been commingled with gas purchased from other sources. In an effort to harmonize that result with the statutory language, the court concluded that an intracorporate transfer of gas from a pipeline's production division to its transmission division is a "first sale" within the meaning of the NGPA. Several respondents have advanced the alternative argument that the Commission must

accord "first sale" treatment to a fixed portion of each downstream sale from a pipeline's mixed system supply based on the ratio of the pipeline's own production to its total system supply. We believe neither of these approaches is correct. It is our submission that the construction provided by the Commission—the agency charged with administering and enforcing the statute—is the most reasonable one, and that the court of appeals erred in rejecting it.

A. The Commission's Interpretation is Strongly Supported by the Literal Language of Section 2(21)(B) of the Act

As in all cases involving statutory construction, "we begin with the language of the statute itself" (*Howe* v. *Smith*, 452 U.S. 473, 480 (1981)), and we assume that "the legislative purpose is expressed by the ordinary meaning of the words used." *Richards* v. *United States*, 369 U.S. 1, 9 (1962). Thus, "[a]bsent a clearly expressed legislative intention to the contrary, that language must ordinarily be regarded as conclusive." *Consumer Product Safety Commission* v. *GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980). See *American Tobacco Co.* v. *Patterson*, No. 80-1199 (Apr. 5, 1982), slip op. 5. The language of Section 2(21)(B) strongly supports the Commission's construction.

1. Section 2(21)(A) of the NGPA defines a "first sale" as any sale of natural gas *to* a pipeline, a local distribution company, or any person for use by such person. Section 2(21)(B), however, specifically excludes from the definition of "first sale" any sale *by* an interstate or intrastate pipeline, a local distribution company, or any affiliates thereof,

> unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

Thus, the statute on its face establishes the general rule that pipeline sales are not "first sales."

A particular sale of pipeline produced gas may only escape this general exclusion if the sale is "attributable" to the pipeline's own production. The Commission reasoned (Pet. App. B-61 to B-62) that because the term "attributable" qualifies "such sale," *all volumes subject to the sale*

must be comprised of gas produced by the pipeline in order for the sale to be "attributable" to the pipeline's production. A sale by a pipeline from its mixed system supply downstream of the wellhead cannot be "attributable" to the pipeline's own production, because such a sale is comprised of gas from various sources.

2. Those respondents that contend that the Commission construed the statute too narrowly in denying "first sale" status to downstream sales would read into the statute words that were not put there by Congress. Section 2(21)(B) does not state "unless *a portion (or a pro rata share) of* such sale is attributable to volumes of gas produced by [a pipeline]." Instead, Congress specifically stated "unless *such sale* is attributable" to the pipeline's own production. As the court of appeals correctly concluded (Pet. App. A-8), Section 2(21)(B) bars a mixed system sale from being accorded "first sale" treatment:

> If [the] denial [in the first part of Section 2(21)(B)] of "first sale" status to pipeline sales had not been included in the NGPA, pipelines which bought gas produced by independent producers and then resold it would have been involved in two "first sales," once as purchaser from the independent producer and then as seller to its [resale] customer. The restriction operates to eliminate this possibility by denying "first sale" status to the downstream sale.

This reading of Section 2(21)(B) is confirmed by other provisions of the NGPA. Thus, when Congress meant to limit the applicability of certain provisions, it used "attributable" in conjunction with qualifying language. For example, Section 110(a)(1), 15 U.S.C. (Supp. V) 3320(a)(1) (emphasis added), provides that a first sale price may exceed the maximum lawful price if the excess is necessary to recover

> State severance taxes *attributable* to the production of such natural gas and borne by the seller, *but only to the extent* the amount of such taxes does not exceed the limitation of subsection (b) * * *.

To like effect, Section 503(e)(2)(B), 15 U.S.C. (Supp. V) 3413(e)(2)(B) (emphasis added), which allows a seller of natural gas to charge a special rate under the NGPA pending a determination whether the seller is entitled to that or a higher rate, authorizes the Commission to take measures

> to provide adequate assurance that funds, *to the extent attributable* to a price in excess of the appropriate maximum lawful price under [Title] I * * * are available in the event of such refund.

Congress' failure similarly to modify "attributable" in Section 2(21)(B) reflects its intention that, in the context of that section, "attributable" means, as the Commission held, "exclusively comprised of." The only sale of gas by a pipeline that is exclusively comprised of pipeline production is a sale at the wellhead or its functional equivalent—i.e., where "the pipeline commit[s] volumes of gas from an identifiable well to a particular purchaser and subsequently [withdraws] equivalent volumes from system supply for sale to the purchaser" (Pet. App. B-53 n.5; see also *id.* at B-3).[18]

3. Moreover, the language of the statute offers no support for the court of appeals' conclusion that Congress meant to require the Commission to treat the physical movement of gas from a pipeline's producing division to its transmission division—i.e., an intracorporate transfer—as a "first sale." To begin with, in order for such a transfer to qualify as a "first sale," it must first constitute a "sale." Section 2(20) of the NGPA, 15 U.S.C. (Supp. V) 3301(20),

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[18] The court of appeals incorrectly viewed this identifiable downstream sale to a particular purchaser as inconsistent with the Commission's wellhead sale analysis (Pet. App. A-10). However, such a sale is tantamount to a producer sale, in which a local distribution company buys gas in a first sale directly from a producer at the wellhead and has the gas transported by a pipeline and delivered from the pipeline's general system supply. A similar arrangement can be made between a distributor and a pipeline producer. In either situation, the sale is governed by a contract that commits gas from particular wells, leases or other producing properties, and is for all intents and purposes a wellhead-type sale. On the other hand, any other sale by a pipeline from its general system supply is not so tied to production from any particular well, lease or other property.

defines "sale" as "any sale, exchange, or other transfer for value." It thus is clear that for any transfer or exchange of gas to come within the statutory definition, it must be for "value," i.e., for a fair consideration. See *Black's Law Dictionary* 1391 (5th ed. 1979) (defining "value" as "[a]ny consideration sufficient to support a simple contract"). As the Commission noted, however, intracorporate transfers involve merely "bookkeeping and accounting entries of a corporation rather than * * * actual sales" (Pet. App. B-5; see *id.* at B-66). There is no transfer of cash or other consideration and no change of title. In short, an intracorporate transfer has none of the traditional and usual indicia of a sale.

Consistent with this notion, a "sale" under the Uniform Commercial Code similarly requires an exchange of consideration. U.C.C. ¶ 2-106(6); see R. Anderson, *Anderson on the Uniform Commercial Code* ¶ 2.106:6 (3d ed. 1981). Accordingly, the simple transfer of a commodity from one division of a corporation to another is not considered a transfer for value because ownership remains within the same corporate entity—only the physical location of the commodity changes.[19]

This same approach traditionally has governed transactions under the Natural Gas Act. For example, a transportation agreement between a gas producer and a pipeline does not constitute a "sale" under the Natural Gas Act, since "[a]n essential ingredient of an exchange is a transfer of title ***." *Public Service Electric & Gas Co.* v. *FPC*, 371 F.2d 1, 4 (3d Cir. 1967). In addition, a sale under the Natural Gas Act must be governed by a contract and a certificate of public convenience and necessity.[20]

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[19] The courts have held that the transfer of a commodity within a single corporation is not a sale, since such a transfer involves neither a transfer of title nor an exchange of consideration. See *Utah Concrete Products Corp.* v. *State Tax Commission*, 101 Utah 513, 520-521, 125 P.2d 408, 412 (1942); *Coulter Electronics, Inc.* v. *Department of Revenue*, 365 So.2d 806, 808-809 (Fla. Dist. Ct. App. 1978). Cf. *Carlton* v. *United States*, 385 F.2d 238, 242 (5th Cir. 1967).

[20] As to the requirement of a contract, see 15 U.S.C. 717c(c),and (d); *United Gas Co.* v. *Mobile Gas Corp.*, 350 U.S. 332, 345 (1956) ("The Natural Gas Act * * * recognizes the need for private contracts of varying terms and expressly provides for the filing of such contracts as a

Intracorporate transfers of pipeline production have never been subject to these traditional requirements precisely because they have never been viewed as "sales" under that Act.

Nor did Congress manifest any intent to depart from these traditional commercial principles in its definition of "first sale" in the NGPA.[21] Thus, Section 2(21) itself is de-

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part of the rate schedules"). As to the requirement of a certificate of public convenience and necessity, see 15 U.S.C. (& Supp. V) 717f(c); *Sunray Mid-Continent Oil Co.* v. *FPC*, 364 U.S. 137, 156 (1960) ("An initial application of an independent producer, to make movements of natural gas in interstate commerce, leads to a certificate of public convenience and necessity * * *.").

[21] On two prior occasions, Congress used the term "first sale," but this earlier usage offers little guidance in construing the term as used in the NGPA. In the Emergency Petroleum Allocation Act of 1973, 15 U.S.C. (& Supp. V) 751 *et seq.* (EPAA), Congress authorized the President to set allocation and price rules for a "first sale" of petroleum products. In Section 403(d) of the Department of Energy Organization Act, Pub. L. No. 95-91, 91 Stat. 585, the Commission was empowered to permit parties to serve written interrogatories upon one another in a rulemaking involving the "charges for the 'first sale' of natural gas by a producer or gatherer to a natural gas pipeline under the Natural Gas Act." In both statutes the term "first sale" was not defined.

In implementing the EPAA, the Federal Energy Administration exercised its discretion to define "first sale" so as to prevent circumvention of EPAA ceiling prices. Thus, a company that both produced its own petroleum and purchased oil from others for resale could charge whatever the market allowed for that portion of the total volumes sold that came from its own production—which was deemed to be involved in a "first sale"—but was limited to ceiling prices for the remaining volumes. *Marvin E. Boyer Co.*, 3 F.E.A. ¶ 83,088 (1976). Here, as we show below (pages 27-28, *infra*), Congress similarly empowered the Commission to permit "first sale" status to be imputed where necessary to prevent circumvention of NGPA prices, but the Commission in the exercise of its discretion has determined that imputing "first sale" status to pipeline intracorporate transfers of gas is neither necessary nor appropriate. Moreover, the EPAA did not contain any limitation on the term "first sale"; in contrast, the NGPA specifically precludes "first sale" treatment for any pipeline sale "unless such sale is attributable to" the pipeline's own production. In the DOE Act, a "first sale" specifically refers only to a sale from a producer or gatherer to a pipeline. There is no reference in that Act to a pipeline's sales of its own production and no indication that Congress intended to encompass such sales.

void of any reference either to an "intracorporate transfer" or to the various divisions (e.g., production and transmission divisions) of a single corporate entity. On the contrary, the only entities referred to in the statute are "interstate pipelines, intrastate pipelines, local distribution companies and affiliates thereof."[22] In short, giving the terminology used by Congress its "ordinary" and "common" meaning (*Perrin* v. *United States*, 444 U.S. 37, 42 (1977)) leads inescapably to the conclusion that Congress did not intend to grant automatic "first sale" status to the transfer of gas between the production and transmission divisions of a pipeline.

Both the court of appeals' "intracorporate transfer" theory and respondents' "downstream sales" theory proceed from the erroneous premise that "Congress clearly intended for any [pipeline] production *** to be accorded first sale status under the NGPA" (Pet. App. A-15). As our examination of the language of Section 2(21)(B) has shown, however, Congress did not manifest any such intent in its definition of "first sale." Thus, the major defect in the interpretations proferred by the court of appeals and respondents is that they disregard the settled principle that the plain language of a statute is usually the best guide of legislative intent. Because that language strongly supports the Commission's interpretation, there is no need to look further. Nevertheless, other available indicia of Congress' intent also support the Commission's position.

In sum, as used in each of these prior statutes, the term "first sale" had discrete and independent meanings. Furthermore, both earlier statutes were enacted to serve functions entirely distinct from the goals of the NGPA.The term "first sale" is specifically defined in the NGPA, and that definition does not incorporate or refer either to the EPAA or the DOE Act. Finally, nothing in the legislative history of the NGPA suggests that Congress intended either the EPAA or the DOE Act to guide construction of the term "first sale" as it appears in Section 2(21) of the NGPA.

[22] In addition, the definitions of these entities in the NGPA focus solely on the transportation of natural gas, without reference to production. For example, an "interstate pipeline" is defined as "any person engaged in natural gas *transportation* subject to the jurisdiction of the Commission" under the Natural Gas Act. 15 U.S.C. (Supp. V) 3301(15) (emphasis added). Moreover, the definitions of "affiliate" and "person" under the Act clearly contemplate separate and formal entities. See 15 U.S.C. (Supp. V) 3301(26), and (27).

B. The Structure And History of the NGPA Fully Support the Commission's View

1. The Commission's reading of the literal language of the statute is confirmed by the structure of the Act. Thus, Congress placed the incentive prices for "first sales" of gas in Title I of the NGPA, which it named "Wellhead Pricing." The term "wellhead sales" generally refers to sales made in the field by producers to pipelines. See, e.g., *Maryland* v. *Louisiana*, 451 U.S. 725, 730 (1981) ("Most often, the producer sells the gas to the pipeline companies at the wellhead * * *"). If there were any doubt as to the meaning of the language used by Congress in defining a "first sale," the structure of the Act removes that doubt by linking "first sale" with "wellhead prices." A statutory title can assist in clarifying ambiguities in the statute[23] and, to the extent that the meaning of Section 2(21)(B) may be regarded as uncertain, the title legitimately aids here in clarifying the legislative intent. The reference to "Wellhead Pricing" supports the Commission's conclusion that the statutory pricing scheme reflects "a distinction between a pipeline['s] * * * producer or field sales, and other sales that remain subject to Commission or state jurisdiction" (Pet. App. B-52).

Moreover, Title VI of the NGPA, entitled "Coordination with the Natural Gas Act," defines in detail the relationship of the NGPA to the preexisting regulatory framework under the Natural Gas Act. While the Commission's Natural Gas Act jurisdiction is carefully limited in certain specific respects, Title VI fails to suggest any intent by Congress to repudiate the Commission's traditional treatment under the Natural Gas Act of pipeline production placed in system supply.[24]

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[23] See *Chemehuevi Tribe of Indians* v. *FPC*, 420 U.S. 395, 403-404, 413 (1975); 2A *Sutherland Statutory Construction* § 47.03, at 73 (C. Sands rev. 1973).

[24] The NGPA leaves intact the Commission's existing authority under the Natural Gas Act to regulate sales for resale by interstate pipelines. Section 601 of the Act, 15 U.S.C. (Supp. V) 3431, limits the Commission's jurisdiction under the Natural Gas Act only over prices

That Congress meant no sharp break from forty years of regulatory history is underscored by Section 601(b)(1)(E), 15 U.S.C. (Supp. V) 3431(b)(1)(E). That section provides that the price of gas in first sales between an "interstate pipeline and its affiliate" will be deemed just and reasonable if it does not exceed the amount paid in comparable sales between persons not affiliated with interstate pipelines. The plain import of this provision is to safeguard against the possibility that affiliated companies might ignore market realities in contracting for maximum lawful rates. The section, however, makes no mention of intracorporate transfers. It seems fair to conclude—given Congress' concern with price fixing between related entities—that this omission was not inadvertent. Rather, it indicates that Congress did not contemplate that an intracorporate transfer would be deemed a "first sale" as a matter of statutory right; for if Congress had so contemplated, it surely would have inserted similar language limiting intracorporate transfers to prevailing market rates.[25]

2. The legislative history relating to the term "first sale" also supports the Commission's view. Thus, the House Report on the proposed legislation clearly reflects Congress' understanding that the term "first sale" refers to an off-system sale at the wellhead:

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paid in certain first sales and guarantees that pipelines may pass through to their customers these first sale prices. It is only to this limited extent that the Commission's traditional ratemaking authority over pipeline sales for resale is affected.

[25] The correctness of this conclusion is underscored by the fact that Section 5 of the Senate bill (S. 2104, 95th Cong., 1st Sess. (1977), as amended by Section 206 of the Bentsen-Pearson amendment (see 123 Cong. Rec. 30186 (1977)), the counterpart of Section 601(b)(1)(E), contained an "affiliated entities limitation" that included pipeline production. That section would have provided that where a pipeline "purchases new natural gas from an affiliate *or produces new natural gas from its own properties*" (emphasis added), the pass-through of that cost to the pipeline's customers would be limited to prices prevailing for equivalent sales between nonaffiliated persons. This reference to pipeline production was deleted in conference.

Maximum Lawful Price—First Sale Concepts

Part D establishes "maximum lawful prices" applicable to certain categories of "first sales" of natural gas under natural gas sales contracts. *The Committee intends that the term "first sales" be applied by the Federal Power Commission to the first transfer of natural gas for value in an arms-length transaction. Therefore, the first sale price is essentially a wellhead price.*

H.R. Rep. No. 95-496 (Pt. 4), 95th Cong., 1st Sess. 103 (1977) (emphasis added).[26]

Neither the court of appeals' conclusion that Congress intended a "first sale" to encompass an intracorporate transfer, nor the alternative theory that a "first sale" necessarily includes a downstream sale from a pipeline's mixed system supply, can be squared with this unequivocal expression of congressional intent that "first sale" means an actual sale of gas in the field. This point is reinforced by the explanation of the Conference Report on the floor of the House by Congressman Dingell, Chairman of the Subcommittee on Energy and Power of the House Committee on Interstate and Foreign Commerce, and a leading proponent of the legislation in the House. Representative Dingell referred to the statutory price as "generally applicable to field sales * * *." 124 Cong. Rec. 38362 (1978).[27]

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[26] At another point, the House Report used "wellhead sale" as synonymous with the statutory term "first sale": "[T]he Federal Power Commission is authorized to establish adjustments in the *first sale (wellhead)* price * * * ." H.R. Rep. No. 95-496 (Pt. 4), *supra*, at 103 (emphasis added).

[27] Additional evidence of Congress' intent concerning the scope of a "first sale" is provided by the rejection of a proposal under which all new gas, including all pipeline produced gas, would automatically have qualified for higher prices. The Senate Bill that was sent to conference would have decontrolled prices for all new gas "*sold or delivered* in interstate commerce for the first time after January 1, 1977." S. 2104, 95th Cong., 1st Sess. (1977), as amended by Section 204(7) of the Bentsen-Pearson amendment (123 Cong. Rec. 30186 (1977)) (emphasis added). This language was deleted in conference; as ultimately enacted, the statute limits application of the incentive pricing provisions to situations involving a "first sale" of gas rather than mandating NGPA prices for all pipeline gas "sold or delivered." Deletion of the "sold or delivered" language by the Conference Committee "'militates

3. To be sure, there is little discussion in the debates and other relevant legislative sources focusing on this subject specifically on pipeline production. But the relative silence in the legislative record supports the Commission's interpretation of the scope of a "first sale" under the NGPA.

It is clear that in enacting the Natural Gas Act Congress was concerned principally with the regulation of pipelines, not independent producers. See *Phillips Petroleum Co.* v. *Wisconsin*, *supra*, 347 U.S. at 688-689 (Douglas, J., dissenting). It is also clear that under the Natural Gas Act the Commission consistently had regulated pipeline production as an integral aspect of a pipeline's transmission business, and, for rate purposes, had treated the transmission and sale by a pipeline of its own production as "one wholesale * * * transaction." *In re Columbian Fuel Corp.*, *supra*, 2 F.P.C. at 206. It was only in 1954, after this Court's decision in *Phillips*, that the Commission began to regulate the production and gathering operations of independent producers under the Natural Gas Act—and then in a manner different from its regulation of pipeline production (see pages 3-5, *supra*).

In Title I of the NGPA, Congress sought to effect significant modifications in the regulatory scheme that had emerged after *Phillips*. In so doing, it embarked upon a new incentive pricing approach primarily directed at wellhead sales of gas by independent producers.[28] At the same time, however, Congress kept intact the Commission's traditional authority under the Natural Gas Act to set rates

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against a judgment that Congress intended a result that it expressly declined to enact.'" *North Haven Board of Education* v. *Bell*, No. 80-986 (May 17, 1982), slip op. 16, quoting from *Gulf Oil Corp.* v. *Copp Paving Co.*, 419 U.S. 186, 199-200 (1974).

[28] Thus, the House bill stated that one of the purposes of the proposed legislation was

> * * * to bring the natural gas market into better balance by reducing the demand for natural gas and increasing the supply through the establishment of a uniform and incentive-based pricing system for new natural gas which provides fair and equitable *producer* revenues and protects consumers * * *.

H.R. 8444, Section 401(b)(2), 95th Cong., 1st Sess. (1977) (emphasis added).

for pipeline sales of gas for resale in interstate commerce. See *Columbia Gas Development Corp.* v. *FERC*, 651 F.2d 1146, 1157 n.14 (5th Cir. 1981). In this setting, it would have been unnecessary for Congress to discuss pipeline production in any detail unless it meant to change the regulatory status of pipeline production. Although this Court has cautioned that the "silence of Congress may provide a treacherous guide to its intent," we submit that "it is almost inconceivable that Congress knowingly would have [disavowed Natural Gas Act regulation of pipeline production with respect to anything other than sales at the wellhead] without a word of comment." *Watt* v. *Alaska*, 451 U.S. 259, 271 n.13 (1981).

4. The legislative materials relied upon by the court below for its contrary view are not persuasive. First, the court pointed to a provision in Title II of the Act, which deals with incremental pricing (Pet. App. A-11 to A-12). In order to mitigate the consumer impact of the increased wellhead prices under Title I, Title II generally provides for the pass-through of the greatest portion of these increased costs to a discrete group of customers—certain industrial users. For these purposes, each pipeline is required to determine the cost of acquiring the gas it sells; the amount of these acquisition costs in excess of a specified threshold is isolated in a separate account and that amount is passed through to the industrial users (until such users are paying the same price they would be paying for alternative fuel). Thus, for purposes of Title II, the "acquisition cost" of gas is just that: the pipeline's cost of acquiring the gas.

Title II describes these acquisition costs as "first sale acquisition costs." Section 203, 15 U.S.C. (Supp. V) 3343, provides two rules for determining a pipeline's acquisition costs for purposes of incremental pricing. First, Section 203(b)(1), 15 U.S.C (Supp. V) 3343(b)(1) provides generally that the "first sale acquisition cost" will be the price paid for gas "acquired in [a] first sale." However, Congress found it necessary to create a special rule for interstate pipeline production: "For purposes of this section, in the case of any natural gas produced by an interstate pipeline * * * the first sale acquisition cost of such natural gas shall be determined in accordance with rules prescribed by the

Commission." Section 203(b)(2), 15 U.S.C. (Supp. V) 3343(b)(2). As the Commission observed, this provision "differs notably from the general rule in that it omits any reference to 'price paid' and does not indicate that such gas will be 'acquired in a first sale'" (Pet. App. B-68).

These differences do not, however, establish that an intracorporate transfer must be regarded as a "first sale" in the very different context of Title I. An explanatory statement prepared by several principal sponsors of the NGPA in the House of Representatives specifically states that "the language [of] * * * section 203(b)(2) is limited in its applicability to * * * Title II." 124 Cong. Rec. 38367 (1978). Furthermore, if the court's intracorporate transfer theory is correct, Section 203(b) would have been entirely superfluous. If Congress had intended an intracorporate transfer automatically to constitute a "first sale" for the purpose of triggering the pricing provisions of Title I, there would have been no need for any special rule empowering the Commission to determine the amount of pipeline production acquisition costs.

Equally wide of the mark is the reliance by the court below on the language of the Conference Report construing the Commission's rulemaking authority under Section 501 of the Act, 15 U.S.C (Supp. V) 3411. That Report states only that

> * * * *the Commission* may define terms such as "transfer for value" used in the definition of first sale; it *may also establish rules applicable to intracorporate transactions under the first sale definition.*

H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 116 (1978) (emphasis added). The court of appeals apparently read the phrase "under the first sale definition" as qualifying "intracorporate transactions." Accordingly, the court concluded that "[t]his comment assumes that intracorporate transactions will fall within the first sale definition. The decision which Congress committed to the Commission's judgment was whether regulations were necessary to govern those transactions" (Pet. App. A-12 to A-13). We disagree. The court overlooked the fact that in Section 2(21)(A)(v) of the NGPA, Congress authorized the Commission to define

any sale as a "first sale" "in order to prevent circumvention of any maximum lawful price established" under Title I. Thus, the more reasonable interpretation of the Conference Report is that, by granting to the Commission the authority to define an intracorporate transfer as a "sale," and thus as a "first sale," Congress simply meant to provide the Commission with the means by which to implement its discretionary authority to foreclose circumvention under Section 2(21)(A)(v).[29] The court's reading, on the other hand, adds a new and unsupported dimension to the statutory language. Surely, if Congress had intended a "first sale" automatically to include an "intracorporate transfer," it would have expressed that intent in a more direct manner.

C. The Commission's Analysis is Consistent With the Policies Underlying the NGPA

The court of appeals correctly identified two of the principal purposes of the NGPA: (1) to create a unified market for natural gas; and (2) to provide incentive prices for the production of new gas. Contrary to the court's view, the Commission's analysis is not inconsistent with either of these statutory goals.

1. *The Commission's approach will not perpetuate a dual market for interstate and intrastate gas or discourage increased production*

There is no evidence that Congress viewed elimination of the dual market structure or the need to promote increased production as requiring across-the-board incentive pricing for all pipeline production. Pipeline production had, at best, only a marginal impact on the dual market problem. Re-

[29] For example, the court of appeals was concerned that to adopt the Commission's interpretation would "be to leave intact state regulation of intrastate pipeline and local distribution company production * * * [and] thus * * * perpetuate * * * the dual market structure Congress sought to eliminate" (Pet. App. A-10). Even assuming that the court was correct as to the impact of this interpretation on the marketplace (but see pages 29-30, *infra*), the Commission could remedy this impact by defining an intracorporate transfer as a "first sale" (see Pet. App. B-6 to B-8)).

gardless of the disparity in prices between intrastate and interstate markets, pipelines were not "shopping the marketplace," as were independent producers, in order to command the highest price for their gas. On the contrary, they were seeking in general to maintain sufficient reserves for their own system needs, whether interstate or intrastate. Accordingly, the court of appeals erred in concluding that if most production by intrastate pipelines and local distribution companies were not regulated under the NGPA the result would be the perpetuation of bifurcated markets; this conclusion assumes that unregulated intrastate pipelines would somehow extend their operations into the interstate market. But nothing in the NGPA suggests that Congress saw a need to alter pipeline distribution routes; instead, it is more reasonable to conclude that Congress believed that interstate pipelines would continue to serve the interstate market while intrastate pipelines would continue to serve their state markets.

To be sure, encouragement of pipeline exploration and production through incentive pricing would operate to increase the supply of gas in whichever market a pipeline operates. But pipelines are only secondary sources of gas supply, and then primarily for their own systems. The basic congressional objective in the NGPA was to encourage exploration and development by independent producers, who provide supplies of gas to all systems, both interstate and intrastate. As construed by the Commission, Section 2(21)(B) serves this objective. Thus, an off-system sale of pipeline produced gas at the wellhead is a "first sale" entitled to NGPA incentive pricing because in such a transaction, which ordinarily involves a sale to another pipeline, the producing pipeline acts just like an independent producer. Accordingly, permitting the pipeline to price its production at NGPA levels for these producer-type transactions can aid in eliminating the bifurcated market.[30] There is no

[30] A central assumption underlying the decision of the court of appeals is that pipeline producers do not engage in any off-system wellhead sales; the court therefore believed that under the Commission's interpretation of Section 2(21)(B) the "unless" clause of that statute would be rendered a "nullity" (Pet. App. A-8). The court's assumption

similar functional equivalence or market impact when a pipeline producer transports and sells gas to its traditional customers as part of its system supply.

2. The Commission properly recognized that the policies underlying the NGPA do not require that pipeline producers be treated in all instances identically to independent producers

a. The court of appeals erroneously assumed that Congress intended that there be no "distinction between pipeline and independent producers" and that "pipeline producers deserve the price encouragement of NGPA no less than other producers" (Pet. App. A-9). Contrary to the understanding of the court below, there is no evidence that Congress intended the Title I pricing scheme to apply without distinction to pipeline producers and independent producers—or, for that matter, that *all* gas was automatically to receive incentive pricing under Title I. Instead, the relevant legislative materials show that Congress carefully sought to tailor the application of incentives to those categories of gas for which incentives would have a stimulating effect on gas production. The NGPA establishes ceiling prices that no one may lawfully exceed; it does nothing to limit or discourage establishment of prices below the ceiling. Prices may be fixed below the ceiling either by contractual commitment or state regulations.

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is unfounded. Pipelines in fact do make off-system sales of their own production at the wellhead. See, e.g., 50 F.P.C. 727 (1973); 17 F.E.R.C. ¶ 63,007 (1981). See also "FERC Form No. 2: Annual Report of Natural Gas Companies (Class A and Class B)," filed by El Paso Natural Gas Company for the year ending Dec. 31, 1981, at 311-10 to 311-18, reprinted in the Appendix, *infra*, 1a-10a. (In the left-hand column, entitled "Name of Other Gas Utility," the pipeline lists a substantial number of wellhead sales.) Furthermore, these producer-type sales are afforded "first sale" status under the Commission's interpretation of NGPA Section 2(21)(B). See 18 C.F.R. 270.203(a). Undeniably, such sales are hardly comparable in volume or number to independent producer sales; but that is simply because pipelines—unlike independent producers—are basically in the business of serving the needs of their system customers.

In Section 602(a), 15 U.S.C. (Supp. V) 3432(a), for example, Congress specifically provided that a state may continue to set rates for a "first sale" of gas produced and sold within the state, provided those rates do not exceed NGPA ceiling prices.[31] Furthermore, independent producers are limited to the prices prescribed by their contracts. As the Conference Report explained, "maximum lawful prices are ceiling prices only. In no case may a seller receive a higher price than his contract permits." H.R. Conf. Rep. No. 95-1752, *supra*, at 74. See Section 101(b)(9), 15 U.S.C. (Supp. V) 3311(b)(9). In short, "the conferees attempted to focus producer incentives onto those categories of natural gas where increased discovery and production appear most feasible." Staff of Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 2d Sess., *Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978*, at 8 (Comm. Print No. 95-62, 1978). See 124 Cong. Rec. 38360-38361 (1978) (remarks of Rep. Dingell) (focus of NGPA is on categories of production promising "the greatest supply response at the lowest cost to consumers"). See also *Pennzoil Co.* v. *FERC*, 645 F.2d 360, 374-376 (5th Cir. 1981), cert. denied, No. 81-340 (Jan. 11, 1982)[32]

Under this approach, independent producers do not inevitably qualify for full incentive pricing where their contracts prescribe a lower price.[33] It would be anomalous in

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[31] Section 602(a) states: "Nothing in this chapter shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under subchapter I of this chapter."

[32] Indeed, the Fifth Circuit itself has pointed out that "the NGPA did not intend indiscriminate application of the incentive." *Columbia Gas Development Corp.* v. *FERC*, *supra*, 651 F.2d at 1160. Instead, that court has recognized that incentive pricing rests on the notion that "availability of a higher price [is] *necessary* to spur production * * *." *Pennzoil Co.* v. *FERC*, 671 F.2d 119, 123 (1982) (emphasis in original).

[33] As regards gas sold by independent producers from existing wells from which gas flowed in interstate commerce prior to enactment of the NGPA, no incentive is required. Accordingly, in Section 104 of the Act, 15 U.S.C. (Supp. V) 3314, Congress provided that the maximum

the extreme to conclude that Congress nonetheless meant to permit pipeline producers to qualify automatically for full NGPA prices by virtue of "intracorporate transfers" that are not governed by contracts or by other indicia of a commercial transaction.

b. At the time of the enactment of the NGPA, pipeline production sold through a pipeline's own system was subject to Commission valuation on two distinct bases: cost of service or independent producer parity, with the major division between the two types of treatment turning on date of lease acquisition or well drilling. On the other hand, pipeline production sold off-system directly from a producer-pipeline's own well (i.e., at the wellhead) was priced at parity irrespective of lease or well date. In short, where pipeline producers performed in a manner functionally equivalent to independent producers, they uniformly were granted incentives in the same manner as independent producers—those operating below the assumed average cost levels earned a greater return, while those operating at higher than average costs earned a lower return. Conversely, when pipelines transported the gas which they themselves produced and sold that gas downstream from mixed system supply, they were treated not as producers but as pipelines deemed to be involved in "one wholesale * * * transaction." *In re Columbian Fuel Corp., supra*, 2 F.P.C. at 206.

As construed by the Commission, the NGPA itself makes no substantive change in this regulatory structure: pipeline produced gas sold off-system at the wellhead in a producer-type sale is a "first sale" entitled to Title I pricing; pipeline

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lawful price for such gas is the just and reasonable rates set by the Commission's area and national rate orders, escalated monthly for inflation. The legislative history shows that "[n]arrowing the definition of new natural gas to exclude other categories that would be produced even without deregulation was perceived as a necessity to eliminate unjust enrichment of producers while also lowering consumer costs of deregulation." Staff of Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess., *Economic Analysis of Natural Gas Policy Alternatives*, at 10-11 (Comm. Print No. 95-31, 1977).

production placed in system supply does not qualify automatically for NGPA prices. In exercising its broad discretion under the Natural Gas Act, however, the Commission has granted NGPA pricing to those producers that previously had been receiving independent producer prices under the area or national rates, in order to strengthen system supply by enhancing their ability to compete with independent producers in the "continued development and additional production of natural gas" (Pet. App. B-25). At the same time, those pipeline producers that traditionally had been accorded cost of service treatment so that they could engage in "exploration and production activities while passing on the costs and risks of that investment to [their] purchasers" (*id.* at B-73) were continued on that basis.

The reasons for this difference in treatment are self-evident. Under an incentive pricing system, a producing company can only hope that the applicable maximum price established by statute (or, prior to the NGPA, by the Commission's area or nationwide rate orders) is sufficient to cover the cost of unsuccessful ventures when it sells the output from its producing wells. If the incentive prices appear sufficiently high, the producer will be encouraged to take the gamble and risk its capital exploring in areas which may prove unproductive.[34]

Cost of service treatment, on the other hand, assures a pipeline producer that it will recover its actual costs of exploration, development and production, and that it will have the opportunity to earn a reasonable return on its investment. Most critically, the pipeline recovers amounts so expended whether or not its efforts are successful. Thus, a pipeline producer whose production is priced on a cost of service basis has no fear of loss which must be overcome by

[34] Indeed, incentive prices are based on recognition of the fundamental principle that risk assumption by investors in the gas industry is directly proportional to the expected return on investment. In *Southern Louisiana Area Rate Cases* v. *FPC*, 428 F.2d 407, 426 n.46 (5th Cir. 1970), for example, the court affirmed a price schedule adopted by the Commission which provided special incentives for new production in recognition of the manner in which these incentives would encourage producers to engage in riskier forms of production.

incentives; the pipeline can be confident that it will recover its costs and earn a profit from both successful and unsuccessful exploration. The only factors involved in the pipeline's determination to invest additional capital, therefore, are the needs of its customers and the relative cost of acquiring sufficient supply elsewhere. The pipeline's decisions regarding whether to increase production would not be influenced by incentive pricing, and incentive pricing is not likely to call forth any new gas.

In short, the only likely effect of extending incentive pricing to cost of service pipeline producers would be to grant them an unjustified "windfall." Even where pipeline producers would not incur substantially higher costs and would not increase their output significantly, they nevertheless would be able to escalate their prices, at least prospectively, to the higher incentive levels of Title I.[35] We submit

[35] The consequences that would flow from the court of appeals' decision can be illustrated by considering the treatment of gas produced by an interstate pipeline from pre-1973 wells on pre-October 8, 1969 leases. That gas has always been valued by the pipeline on a cost of service basis. If cost of service valuation were maintained, the pipeline would continue to be reimbursed by the gas consumer, as it has in the past, for all reasonable costs incurred in producing gas from these wells. These costs include the expense of acquiring the leases, paying royalties, and drilling all wells, including unsuccessful wells (dry holes). Under the decision of the court below, this same pipeline would be allowed, at least prospectively, to value the gas from these old wells at the higher NGPA levels. For several reasons, this would present the pipeline with a substantial windfall.

First, because wells that produce gas which is not eligible for parity pricing are, by definition, old wells, most of the requisite expenditures relating to the wells have already been made by the pipeline and paid for by its customers; the operation of a well in its later years is relatively inexpensive. Second, because they were drilled prior to 1973, most of these wells are substantially depleted and have low rates of production. Therefore, they likely would qualify as stripper wells under NGPA Section 108. Stripper well natural gas is eligible for the highest ceiling prices established in the NGPA. Compare NGPA Sections 102(b) and 103(b) with Section 108(a). Thus, a pipeline that under cost of service rates had been fully recovering its costs at a level as low as 26¢ per MMBtu could escalate its prices up to the current Section 108 price of $3.535 MMBtu (effective January 1, 1983), without incur-

that Congress could not conceivably have intended such an irrational result with such unfair consequences for consumers.[36]

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ring any additional expenses. See 18 C.F.R. 271.101. The additional $3.27 per MMBtu would be pure profit.

It is quite possible that most of the gas currently under cost of service regulation would qualify for stripper well prices. Congress established the Section 108 stripper well prices to give producers an incentive to invest additional capital so as to enhance recovery of gas from nearly depleted wells which otherwise would likely have been abandoned. Cost of service pipeline producers need no such incentives, however, because their cost of service treatment assures them compensation for whatever amount they prudently invest in order to enhance gas recovery from these low producing wells. In short, pipelines would enjoy a substantial windfall in collecting the high stripper well price under NGPA Section 108 for gas from old wells which require little additional expenditure by the pipeline. This result is contrary to the intent of Congress in enacting the NGPA. See 124 Cong. Rec. 38362 (1978) (remarks of Rep. Dingell) ("The Natural Gas Policy Act provides reasonable price incentives, while avoiding windfall profits * * *").

[36] In a closely analogous context, the Fifth Circuit rejected a view of the NGPA that would have allowed an independent producer to obtain an unjustified windfall. In *Columbia Gas Development Corp.* v. *FERC*, *supra*, the Commission determined that independent producers that held "optional procedure" certificates could not collect the higher ceiling rates under the NGPA for gas that remained subject to the Natural Gas Act. The certificate procedure had been developed by the Commission in an effort to stimulate producer production. Thus, under the Commission's regulations, independent producers could sign contracts for the production of gas at rates higher than prevailing area or nationwide ceiling rates when the producer determined that the higher rate was sufficient to justify new drilling. The Commission would then determine in a single proceeding whether the public convenience and necessity justified issuance of the certificate and whether the agreed upon rate was just and reasonable. If it so determined, the agreed upon rate was not subject to challenge in a proceeding under Section 4 of the Natural Gas Act, 15 U.S.C. 717c. In return, the producer would agree to a moratorium on future rate increases with respect to the gas covered by the certificate.

In upholding the Commission's refusal to permit collection of NGPA prices for optional procedure certificated gas, the court stated (651 F.2d at 1157 n.13):

> Petitioners argue that the lack of any express statutory provision dealing with optional procedure certificates, and the lack of any discussion of those certificates in the legislative history, sup-

3. The Commission properly exercised its authority under the Natural Gas Act in permitting sales of parity priced gas to be valued at NGPA levels

The court of appeals noted (Pet. App. A-9) that the Commission, exercising its authority under the Natural Gas Act, had extended NGPA prices to some pipeline producers under its parity pricing policy. See pages 9-11, *supra*. In the court's view, however, the Commission's argument in defense of this action was "sophistic," because "[i]t is not an agency's prerogative to alter a statutory scheme even if its alteration is as good or better than the congressional one. The fact that the agency gives back all or part of what it takes from the law's grant in no way justifies departure from the congressional purpose in the first instance" (*id.* at A-9).

Of course, the court's criticism of the Commission's action falls of its own weight if, as we have shown, the Commission's construction of the NGPA is correct. The Commission was not, as the court's language implies, seeking to retain jurisdiction over the pricing of interstate pipeline production under the Natural Gas Act in the face of a congressional directive in the NGPA withdrawing that jurisdiction. Rather, having rationally determined that the only class of pipeline sales that would constitute a "first sale" within the meaning of the statute was an off-system sale at the wellhead or in the field, the Commission properly concluded that Congress had left to it the "task of harmonizing its statutory mandate to implement the NGPA pricing scheme with its continuing authority under the [Natural Gas Act] to determine the price treatment of [system supply]" (Pet. App. B-24). In carrying out that responsibility, the Commission determined that if "pipeline producers

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ports the view that Congress did not intend the singular treatment of optional procedure sales in Order Nos. 64 and 64-A. Such silence is not supportive of the petitioners, however. It would take express treatment of optional procedure certificate gas for such gas to fall outside the general principles of the NGPA that continue the certificate conditions.

Here, as in *Columbia Gas*, there is no evidence that Congress in the NGPA intended to overturn an established regulatory practice.

were held to pre-NGPA prices, or were subject to a newly established cost-based nationwide rate, they would in many instances be unable to compete with independent producers in acquiring new leases" and, as a result, pipeline customers would be denied "a more certain system of additional supplies" (*id.* at B-25).[37]

The Commission, however, imposed a limitation on the valuation by reference to NGPA prices. In all events, the pipeline may not value its own gas eligible for parity pricing at a level exceeding amounts paid in comparable sales (Pet. App. B-37). See note 15, *supra*. Unlike producers, pipelines are not limited by contract in pricing their own gas. Without the comparable sales limitation, the pipeline could value its gas at a rate higher than what the independent producers could command. Under the court of appeals' decision, no such comparable sales limitation is apparent. The result is that the decision places pipelines in a more favorable position than independent producers, which must negotiate a contract with their purchasers to collect the full NGPA prices.

[37] If a pipeline producer were not allowed NGPA pricing levels for gas eligible for parity pricing, the pipeline would have to value this gas under the applicable area or national rates established by the Commission pursuant to the Natural Gas Act. In such a case, the pipeline would at a minimum be denied the escalation factor tied to inflation that was incorporated by Congress into the area and nationwide rates under NGPA Section 104(b)(1)(A), 15 U.S.C. (Supp. V) 3314(b)(1)(A). See NGPA Section 101(a), 15 U.S.C. (Supp. V) 3311(a); see also 124 Cong. Rec. 38364 (1978) (remarks of Rep. Dingell). The increase authorized by the inflation adjustment is not insubstantial. For example, in January 1982, the differences between the NGPA Section 104 price (which includes the inflation adjustment) and the Natural Gas Act price for gas from a well drilled after 1974 is approximately $0.50/MMBtu. The difference increases monthly. See 18 C.F.R. 2.56a(a)(1), (2) and 271.101. If gas eligible for parity pricing also qualifies for a higher NGPA price (e.g., as stripper well natural gas under NGPA Section 108), the disparity between the applicable Natural Gas Act and NGPA rates is much greater.

In sum, if the Commission was correct that the statutory definition of a "first sale" excludes all pipeline produced gas from pricing under Title I of the NGPA with the exception of pipeline production sold off-system at the wellhead or in the field, then it follows that the Commission acted well within its Natural Gas Act authority in extending "parity pricing" at NGPA levels to those pipelines that in the past had received parity pricing with independent producers under area or national rates.[38]

[38] Respondents read too much into the Commission's 1969 parity pricing policy in arguing that it supports the fiction that intracorporate transfers are "sales." To be sure, for purposes of simplifying pipeline rate proceedings, the Commission has allowed the cost of production valued by reference to area and nationwide rates to be passed through to downstream customers in the same fashion as the cost of gas purchased from independent producers (see Pet. App. B-55 n.9). However, the Commission consistently has viewed this process as involving only "one wholesale * * * transaction" (*In re Columbian Fuel Corp.*, *supra*, 2 F.P.C. at 206), i.e., the actual sale to the pipeline's downstream customers. Thus, there has never been any regulatory focus on the so-called "intracorporate transfer" from the pipeline's producing division to its transmission division.

The mechanism under which these costs are passed through to customers is called, in Commission parlance, a "Purchased Gas Adjustment Clause," or "PGA." See 18 C.F.R. 154.38. A PGA permits semi-annual adjustments to rates to reflect changes in, among other things, the cost of "purchased gas." For the limited purposes of the PGA mechanism, "purchased gas costs" are defined in 18 C.F.R. 154.38(d)(4) n.1 to include the value of a pipeline's own production where a pipeline has been operating on the same basis as an independent producer, i.e., assuming all production risks, and recovering costs only through actual sales of gas under area or national rates.

4. Both the court's intracorporate transfer "first sale" and respondents' downstream "first sale" would create a substantial reworking of state and federal regulatory schemes in ways Congress could not have intended

The "downstream sale" theory advocated by some of respondents, as well as the "intracorporate transfer" theory espoused by both the respondents and the court of appeals, would entail substantial changes in the existing regulatory framework despite the absence of any evidence that Congress intended such a result.

Adoption of the "downstream sale" approach would override the existing division between state and federal regulation of pipeline sales of natural gas. As the Commission pointed out (Pet. App. B-62; see also *id.* at B-4), adoption of the "downstream sale" theory

> would result in the uniform application of first sale maximum lawful prices to all mixed volume retail sales made by pipelines and distributors. * * * The Commission finds no evidence in [Section] 2(21)(B) or in any other provision of the statute that suggests that Congress intended to require the Commission to expand the field of federal ratemaking authority to include all mixed volume retail sales by intrastate pipelines or local distribution companies, the regulation of which has been the historic preserve of the states.

In addition, under either the "downstream sale" theory or the "intracorporate transfer" theory, the natural gas industry may well be faced with uncertainties as to the proper interpretation and application of provisions of the NGPA other than the incentive pricing provisions of Title I. For example, the pipelines might argue that reimbursement for the costs of state severance taxes, compression, gathering, processing, treating, liquefying or transporting gas would no longer be determined under the standards developed

pursuant to the Natural Gas Act, but rather would be computed under the different standards established in Section 110(a) of the NGPA, 15 U.S.C. (Supp. V) 3320(a). (See Pet. App. B-63.) The pipelines might also assert that under Section 601(a) of the NGPA, 15 U.S.C. (Supp. V) 3431(a), the Commission would lose its jurisdiction under the Natural Gas Act over certain production and gathering facilities of interstate pipelines. (See Pet. App. B-68 to B-69.)

Finally, adoption of the "intracorporate transfer" theory would, as the Commission observed (Pet. App. B-5), "extend NGPA first sale jurisdiction to all corporations which produce their own natural gas." Several industrial corporations that consume their own natural gas filed comments with the Commission indicating that "no valid regulatory purpose would be served by extending the Commission's jurisdiction to cover such production" (*id.* at B-6). At the time it enacted the NGPA, Congress indicated its support for industrial self help programs.[39] Development of such programs might be deterred by subjecting company-owned production to the filing and other regulatory obligations of the NGPA.

D. The Court of Appeals Erred in Failing to Defer to the Commission's Interpretation of the Statute

This Court has often noted that "the interpretation of an agency charged with the administration of a statute is entitled to substantial deference." *Blum* v. *Bacon*, No. 81-770 (June 14, 1982), slip op. 10. Thus, a court need not "find that the agency's construction was the only reasonable one or even the reading the court would have reached if the question initially had arisen in a judicial proceeding." *FEC*

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[39] See 15 U.S.C. (Supp. V) 3363(d); 15 U.S.C. (Supp. V) 717f(c)(2)(B).

v. *Democratic Senatorial Campaign Committee*, 454 U.S. 27, 39 (1981). Instead, "the narrower inquiry [is] whether the Commission's [interpretation] was 'sufficiently reasonable' to be accepted by a reviewing court." *Ibid.* Respect for the agency's view is particularly appropriate "when the administrative practice at stake 'involves a contemporaneous construction of a statute by the men charged with the responsibility of setting its machinery in motion, of making the parts work efficiently and smoothly while they are yet untried and new.'" *Udall* v. *Tallman*, 380 U.S. 1, 16 (1965), quoting from *Power Reactor Development Co.* v. *International Union of Electrical, Radio & Machine Workers*, 367 U.S. 396, 408 (1961). As the Fifth Circuit itself has recently observed, "[t]he NGPA's complexity is but one more example of why federal courts show great deference to administrative interpretations of an agency's own statutes and limit their inquiry to whether the agency's actions are authorized and rational." *Ecee, Inc.* v. *FERC*, 645 F.2d 339, 360 (1981).

If the court of appeals had applied these governing principles here, we submit that it would have been compelled to uphold the Commission's interpretation of the Act, for, as we have demonstrated, the Commission's view is supported by the language, structure, history and policies of the Act. In these circumstances, the court below should have deferred to the Commission's expertise and sustained its orders.

The court of appeals gave several reasons for refusing to defer to the Commission (Pet. App. A-7): (1) the Commission's construction was not longstanding; (2) it purportedly did not concern an area particularly within the Commission's expertise; and (3) the Commission had no input into developing the term "first sale." These reasons do not withstand analysis.

Although the Commission's construction was new, the statute itself is of recent vintage. Moreover, while the term "first sale" as used in the NGPA is new to the field of natural gas regulation, Congress, in delegating to the Commission the authority to administer and enforce the NGPA, was well aware that the Commission for many years had

regulated "sales" of gas in interstate commerce under the Natural Gas Act, and Congress clearly intended the Commission to apply its expertise in carrying out its regulatory functions under the NGPA.

Finally, the fact that the Commission did not propose the definition of "first sale" in the Act is an insufficient reason for disregarding the Commission's view. To be sure, where an agency actually drafts the legislation and steers it through Congress, its interpretation merits especially great weight. See *Howe* v. *Smith*, *supra*, 452 U.S. at 485. But that does not mean that an agency must provide evidence of actual participation in the drafting of a particular provision in a statute before its views may be entitled to deference. Rather, when an agency charged with administering a statute issues a substantially contemporaneous construction of that statute, the agency is presumed to be aware of congressional intent (see *National Muffler Dealers Association* v. *United States*, 440 U.S. 472, 477 (1979)), although that presumption may be overcome by a showing that the agency's interpretation is inconsistent with the statutory mandate. See *FEC* v. *Democratic Senatorial Campaign Committee*, *supra*, 454 U.S. at 32. Here, the Commission's construction accords with the intent of Congress. In addition, during the legislative process leading up to enactment of the NGPA there was considerable consultation between the appropriate congressional committees and their staffs and the Commission. See, e.g., 124 Cong. Rec. 38374-38375 (1978) (remarks of Sen. Jackson referring to letter from Commission Chairman Charles B. Curtis conveying the Commission's views concerning its ability to enforce the NGPA). That is all the more reason why the court of appeals shoud have deferred to the Commission's interpretation.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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NOVEMBER 1982

APPENDIX

FERC FORM NO. 2: ANNUAL REPORT OF NATURAL GAS COMPANIES (Class A and Class B)

This report is mandatory under the Natural Gas Act, Sections 10(a) and 16, and 18 CFR 260.2. Failure to report may result in criminal fines, civil penalties and other sanctions as provided by law. The Federal Energy Regulatory Commission does not consider this report to be of a confidential nature.

Exact Legal Name of Respondent (Company)
EL PASO NATURAL GAS COMPANY

YEAR OF REPORT: DEC. 31, 1981

FERC FORM NO. 2 (REVISED 12/81)

2a

EL PASO NATURAL GAS COMPANY
PAGES 310 AND 311 - SALES FOR RESALE - NATURAL GAS (ACCOUNT 483)
YEAR 1981

LINE NO.	NAME OF OTHER GAS UTILITY (DESIGNATE ASSOCIATED COMPANIES) (A)	POINT OF DELIVERY CITY OR TOWN AND STATE (B)	FERC TARIFF RATE SCHEDULE DESIGNATION (C)	MCF OF GAS SOLD APPROXIMATE BTU PER CU. FT. 1041 (A) (D)	REVENUE FOR YEAR (SEE INSTR. 5) (E)	AVERAGE REVENUE PER MCF (IN CENTS) (F)	SUM OF MONTHLY BILLING DEMANDS (G)	PEAK DAY DELIVERY TO CUSTOMERS — DATE (H)	PEAK DAY DELIVERY TO CUSTOMERS — MCF NONCOINCIDENTAL (I)	PEAK DAY DELIVERY TO CUSTOMERS — MCF COINCIDENTAL (J) (G)
1	NEW MEXICO(CONTINUED)									
2	JAL GAS COMPANY, INC.							JANUARY 17	16	11
3	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	BENNETTVILLE, NEW MEXICO	NONE		287.67					
4	NNGD SURCHARGE DOCKET NO. CP76-87		NONE		6.78					
5	SPECIAL SERVICE - SEE NOTE (D)		I-1	2,101	5,366.36	246.05				
6	JAL GAS COMPANY, INC.		FS-10	521	800.63	153.67				
7								JANUARY 18	834	589
8	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	JAL, NEW MEXICO	NONE		11,890.16					
9	NNGD SURCHARGE DOCKET NO. CP76-87		NONE		375.23					
10	SPECIAL SERVICE - SEE NOTE (D)		I-1	89,358	221,687.86	248.08				
11	JAL GAS COMPANY, INC.		FS-10	34,305	52,713.59	153.66				
12								DECEMBER 11	555	315
13	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	MAINLINE & FIELDLINE TAPS, LEA & EDDY COUNTIES, N.M.	NONE		13,557.92					
14	NNGD SURCHARGE DOCKET NO. CP76-87		NONE		237.96					
15	SPECIAL SERVICE - SEE NOTE (D)		I-1	100,995	295,668.20	293.27				
16	JAL GAS COMPANY, INC.		FS-10	16,810	25,215.88	153.66				
17								JANUARY 01	64	62
18	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	MALAGA, NEW MEXICO	NONE		1,089.95					
19	NNGD SURCHARGE DOCKET NO. CP76-87		NONE		29.37					
20	SPECIAL SERVICE - SEE NOTE (D)		I-1	7,999	19,246.57	240.61				
21	JAL GAS COMPANY, INC.		FS-10	2,198	3,377.47	153.66				
22										
23	LAS CRUCES, CITY OF				193,862.88			JANUARY 20	11,091	8,470
24	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	LAS CRUCES, NEW MEXICO	NONE		4,084.91					
25	NNGD SURCHARGE DOCKET NO. CP76-87		NONE		692,121.17	302.14				
26	GENERAL DISTRIBUTION SYSTEM		A&D-RM	229,073	1,270,987.51	253.97				
27	RESIDENTIAL		A-2	500,490	1,846,804.05	249.07				
28	NON-RESIDENTIAL		B-3	741,308	1,722.42	239.89				
29	IRRIGATION		D-3 (E)	718						
30										
31	LORDSBURG, CITY OF				12,615.27			JANUARY 17	1,020	765
32	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	LORDSBURG, NEW MEXICO	NONE		358.69					
33	NNGD SURCHARGE DOCKET NO. CP76-87		NONE		53,587.59	302.14				
34	GENERAL DISTRIBUTION SYSTEM		A&D-RM	17,736	177,963.15	251.02				
35	RESIDENTIAL		A-2	70,896	91,010.76	241.67				
36	NON-RESIDENTIAL		B-3	37,350						
37					74,680.34			MARCH 20	6,752	5,768
38	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	LORDSBURG RESALE FOR POWER PLANT	NONE		691.30					
39	NNGD SURCHARGE DOCKET NO. CP76-87		NONE		330,604.62	302.14				
40	GENERAL DISTRIBUTION SYSTEM		A&D-RM	109,421	2,632,295.97	250.71				
41	NON-RESIDENTIAL		B-3	1,049,934						
42										
43	MOUNTAINAIR, TOWN OF				4,827.71			JANUARY 01	330	330
44	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	MOUNTAINAIR, NEW MEXICO	NONE		173.46					
45	NNGD SURCHARGE DOCKET NO. CP76-87		NONE		8,922.09	302.14				
46	GENERAL DISTRIBUTION SYSTEM		A&D-RM	2,953	77,673.76	248.63				
47	RESIDENTIAL		A-2	31,217	36,911.02	243.52				
48	NON-RESIDENTIAL		B-3	15,157						
49										
50	NAVAJO TRIBAL UTILITY AUTHORITY, THE									
51	SPECIAL SERVICE - SEE NOTE (D)	FOUR CORNERS, NEW MEXICO	I-1	796,198	1,944,988.73	244.28		OCTOBER 22	12,832	2,779
52								FEBRUARY 01	59	52
53	SPECIAL SERVICE - SEE NOTE (D)	FRUITLAND, NEW MEXICO	I-1	9,734	23,526.32	241.69				
54								FEBRUARY 10	1,655	1,352
55	SPECIAL SERVICE - SEE NOTE (D)	SHIPROCK, NEW MEXICO	I-1	240,399	573,815.82	238.69		FEBRUARY 01	384	264
56										
57	GENERAL DISTRIBUTION SYSTEM	TOHATCHI, NEW MEXICO	A&D-RM	10,036	30,322.67	302.14				
58	RESIDENTIAL		A-2	108	757.32-	700.48-				
59	NON-RESIDENTIAL		B-3	50,465	126,133.38	249.99				
60										
61	PENNZOIL PRODUCING COMPANY							DECEMBER 02	730	78 (P)
62	WELLHEAD SALES - SEE NOTES (D) (N)	LEA COUNTY, NEW MEXICO	NONE	53,907	111,010.55	207.86				
63										
64	PHILLIPS PETROLEUM COMPANY							MARCH 01	2	1 (P)
65	WELLHEAD SALES - SEE NOTES (D) (N)	EDDY COUNTY, NEW MEXICO	NONE	84	156.81	186.68				

EL PASO NATURAL GAS COMPANY
PAGES 310 AND 311 - SALES FOR RESALE - NATURAL GAS (ACCOUNT 483)
YEAR 1981

LINE NO.	NAME OF OTHER GAS UTILITY (DESIGNATE ASSOCIATED COMPANIES) (A)	POINT OF DELIVERY CITY OR TOWN AND STATE (B)	FERC TARIFF RATE SCHEDULE DESIGNATION (C)	MCF OF GAS SOLD APPROXIMATE BTU PER CU. FT. 1981 (A) (D)	REVENUE FOR YEAR (SEE INSTR. 5) (E)	AVERAGE REVENUE PER MCF (IN CENTS) (F)	SUM OF MONTHLY BILLING DEMANDS (G)	PEAK DAY DELIVERY TO CUSTOMERS DATE (H)	MCF NONCOINCIDENTAL (I)	MCF COINCIDENTAL (J) (G)
1	NEW MEXICO(CONTINUED)									
2	RIO GRANDE NATURAL GAS ASSOCIATION									
3	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	LAS CRUCES, NEW MEXICO	NONE		53,537.29			DECEMBER 23	3,591	2,738
4	NNOD SURCHARGE DOCKET NO. CP76-87		NONE		1,378.93					
5	GENERAL DISTRIBUTION SYSTEM		AND-NM	83,993	253,625.37	302.18				
6	RESIDENTIAL		A-2	299,307	620,918.09	254.15				
7	NON-RESIDENTIAL		A-3	174,921	435,113.87	248.75				
8	IRRIGATION		A-3 (F)	27,599	66,001.80	239.62				
9										
10	SOCORRO, CITY OF									
11	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	SOCORRO, NEW MEXICO	NONE		22,780.95			JANUARY 19	1,697	1,518
12	NNOD SURCHARGE DOCKET NO. CP76-87		NONE		726.88					
13	GENERAL DISTRIBUTION SYSTEM		AND-NM	35,912	108,584.53	302.18				
14	RESIDENTIAL		A-2	81,075	205,552.38	253.53				
15	NON-RESIDENTIAL		A-3	121,956	297,866.87	244.22				
16										
17	SOUTHERN UNION GAS COMPANY									
18	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	ALAMOGORDO, NEW MEXICO	NONE		4,178,938.16			JANUARY 19	7,050	5,678
19	NNOD SURCHARGE DOCKET NO. CP76-87		NONE		104,386.58					
20	GENERAL DISTRIBUTION SYSTEM		AND-NM	130,027	392,863.58	302.18				
21	RESIDENTIAL		A-2	191,180	460,722.04	240.99				
22	NON-RESIDENTIAL		B-3	582,895	1,452,718.95	249.25				
23										
24	GENERAL DISTRIBUTION SYSTEM	ANACONDA COPPER, NEW MEXICO	AND-NM	48,175	145,555.96	302.18		JANUARY 31	2,046	2,046
25	NON-RESIDENTIAL		B-3	460,552	1,145,895.74	248.80				
26										
27	GENERAL DISTRIBUTION SYSTEM	ANAPRA, NEW MEXICO	AND-TX	11,381	34,369.49	301.99		JANUARY 31	597	597
28	RESIDENTIAL		A-3	8,623	18,616.89	215.90				
29	NON-RESIDENTIAL		B-2	101,625	253,168.50	249.12				
30										
31	GENERAL DISTRIBUTION SYSTEM	ANIMAS, NEW MEXICO	AND-NM	4,516	13,648.65	302.18		JUNE 06	358	112
32	RESIDENTIAL		A-2	25,081-	65,025.32-	259.26				
33	NON-RESIDENTIAL		B-3	84,418	210,830.13	249.77				
34										
35	GENERAL DISTRIBUTION SYSTEM	ANTELOPE PASS, NEW MEXICO	AND-NM	57	172.18	302.00		APRIL 15	13	3
36	RESIDENTIAL		A-2	583-	1,581.48-	268.80				
37	NON-RESIDENTIAL		B-3	1,798	4,481.98	249.28				
38										
39	GENERAL DISTRIBUTION SYSTEM	ANTHONY, NEW MEXICO	AND-TX	9,575	28,915.57	301.99		FEBRUARY 01	367	321
40	RESIDENTIAL		A-3	55,167	136,751.78	247.89				
41	NON-RESIDENTIAL		B-2	3,059	7,642.02	249.82				
42										
43	GENERAL DISTRIBUTION SYSTEM	BAYARD, NEW MEXICO	AND-NM	40,508	122,390.89	302.19		JANUARY 31	2,699	2,699
44	RESIDENTIAL		Q-2	100,478	243,567.56	242.41				
45	NON-RESIDENTIAL		B-3	173,037	431,905.07	249.26				
46										
47	GENERAL DISTRIBUTION SYSTEM	BELEN, NEW MEXICO	AND-NM	119,163	360,039.10	302.19		DECEMBER 29	5,071	4,186
48	RESIDENTIAL		A-2	480,225	1,215,920.52	253.20				
49	NON-RESIDENTIAL		B-3	127,575	319,071.74	250.19				
50										
51	GENERAL DISTRIBUTION SYSTEM	BERINO, NEW MEXICO	AND-NM	3,600	10,876.96	302.19		FEBRUARY 01	197	176
52	RESIDENTIAL		A-2	10,599	25,350.38	239.18				
53	NON-RESIDENTIAL		B-3	27,752	69,195.00	249.33				
54										
55	SPECIAL SERVICE - SEE NOTE (D)	CLOVIS, NEW MEXICO	X-1	3,142,162	7,164,632.01	228.02		FEBRUARY 10	29,819	17,586
56										
57	GENERAL DISTRIBUTION SYSTEM	CULBERSON VALLEY, LORDSBURG, NEW MEXICO	AND-NM	818	2,471.60	302.15		JANUARY 01	28	28
58	RESIDENTIAL		A-2	711-	2,039.55-	285.59				
59	NON-RESIDENTIAL		B-3	6,832	16,058.61	249.61				
60										
61	GENERAL DISTRIBUTION SYSTEM	HOLLOMAN A.F.B., NEW MEXICO	AND-NM	92,299	278,872.19	302.18		JANUARY 20	3,943	3,277
62	NON-RESIDENTIAL		B-3	558,517	1,390,805.98	249.00				
63										
64	GENERAL DISTRIBUTION SYSTEM	DEMING FARM AREA, NEW MEXICO	AND-NM	8,529	25,758.89	302.18		AUGUST 31	1,726	326
65	RESIDENTIAL		A-2	80,258-	199,296.72-	270.69				
66	NON-RESIDENTIAL		B-3	171,293	425,882.33	249.25				

EL PASO NATURAL GAS COMPANY
PAGES 310 AND 311 - SALES FOR RESALE - NATURAL GAS (ACCOUNT 483)
YEAR 1981

LINE NO.	NAME OF OTHER GAS UTILITY (DESIGNATE ASSOCIATED COMPANIES) (A)	POINT OF DELIVERY CITY OR TOWN AND STATE (B)	FERC TARIFF RATE SCHEDULE DESIGNATION (C)	MCF OF GAS SOLD APPROXIMATE BTU PER CU. FT. 1041 (A) (D)	REVENUE FOR YEAR (SEE INSTR. 5) (E)	AVERAGE REVENUE PER MCF (IN CENTS) (F)	SUM OF MONTHLY BILLING DEMANDS (G)	PEAK DAY DELIVERY TO CUSTOMERS DATE (H)	MCF NONCOINCIDENTAL (I)	MCF COINCIDENTAL (J) (G)
1	NEW MEXICO(CONTINUED)									
2	SOUTHERN UNION GAS COMPANY(CONTINUED)									
3	GENERAL DISTRIBUTION SYSTEM	GALLUP, NEW MEXICO	ARD-NM	26,648	80,516.27	302.14		DECEMBER 24	1,068	846
4	RESIDENTIAL		A-2	65,705-	164,466.76-	250.31				
5	NON-RESIDENTIAL		B-3	207,019	516,003.18	249.25				
6										
7	GENERAL DISTRIBUTION SYSTEM	GRANTS, NEW MEXICO	ARD-NM	13,603	41,100.12	302.14		MARCH 26	2,307	428
8	RESIDENTIAL		A-2	412,123-	1,033,953.16-	250.88				
9	NON-RESIDENTIAL		B-3	502,127	1,251,535.73	249.25				
10										
11	SPECIAL SERVICE - SEE NOTE (D)	FRUITLAND-KIRTLAND AREA, NEW MEXICO	X-1	177,569	430,551.80	242.47		DECEMBER 02	1,211	975
12										
13	RESIDENTIAL	HOMESTAKE, NEW MEXICO	A-2	7,017	16,161.66	230.35		FEBRUARY 19	1,218	0
14										
15	GENERAL DISTRIBUTION SYSTEM	MCGREGOR RANGE, NEW MEXICO	ARD-NM	6,229	18,805.21	302.14		DECEMBER 01	284	233
16	NON-RESIDENTIAL		B-3	35,161	86,972.76	247.36				
17										
18	GENERAL DISTRIBUTION SYSTEM	PYRAMID VALLEY, LORDSBURG, NEW MEXICO	ARD-NM	6,090	18,398.33	302.14		FEBRUARY 12	1,181	915
19	RESIDENTIAL		A-2	99,373	117,150.34	237.28				
20	NON-RESIDENTIAL		B-3	141,083	351,662.87	249.26				
21										
22	GENERAL DISTRIBUTION SYSTEM	RED MOUNTAIN AREA, DEMING, NEW MEXICO	ARD-NM	650	1,963.93	302.14		JUNE 02	29	12
23	RESIDENTIAL		A-2	3,972-	8,798.55-	253.30				
24	NON-RESIDENTIAL		B-3	7,318	18,263.60	249.57				
25										
26	GENERAL DISTRIBUTION SYSTEM	RODEO, NEW MEXICO	ARD-NM	975	1,935.12	302.13		AUGUST 31	85	27
27	RESIDENTIAL		A-2	5,333-	14,965.50-	280.62				
28	NON-RESIDENTIAL		B-3	20,553	51,461.36	250.39				
29	IRRIGATION		D-3 (E)	187	430.73	230.34				
30										
31	GENERAL DISTRIBUTION SYSTEM	SILVER CITY, NEW MEXICO	ARD-NM	67,635	204,352.39	302.14		JANUARY 17	3,299	3,291
32	RESIDENTIAL		A-2	331,132	822,183.23	248.29				
33	NON-RESIDENTIAL		B-3	55,030	137,182.78	249.29				
34										
35	GENERAL DISTRIBUTION SYSTEM	TATUM, NEW MEXICO	ARD-NM	443	1,338.68	302.14		MARCH 01	750	88
36	RESIDENTIAL		A-2	16,509	26,348.68	159.60				
37	NON-RESIDENTIAL		B-3	39,387	98,192.26	249.30				
38	IRRIGATION		D-3 (E)							
39										
40	GENERAL DISTRIBUTION SYSTEM	THOREAU, NEW MEXICO	ARD-NM	9,939	30,029.73	302.14		DECEMBER 01	321	249
41	RESIDENTIAL		A-2	38,350	94,758.69	247.09				
42	NON-RESIDENTIAL		B-3	9,487	23,668.22	249.48				
43										
44	GENERAL DISTRIBUTION SYSTEM	TRUTH OR CONSEQUENCES, NEW MEXICO	ARD-NM	45,065	136,159.39	302.14		DECEMBER 01	1,998	1,588
45	RESIDENTIAL		A-2	113,028	300,328.07	265.71				
46	NON-RESIDENTIAL		B-3	180,169	449,567.26	249.26				
47										
48	GENERAL DISTRIBUTION SYSTEM	TYRONE, NEW MEXICO	ARD-NM	6,137	18,542.42	302.14		DECEMBER 01	198	190
49	RESIDENTIAL		A-2	26,184	64,462.41	246.19				
50	NON-RESIDENTIAL		B-3	1,865	4,670.62	250.44				
51										
52	GENERAL DISTRIBUTION SYSTEM	WHITE SANDS MISSILE RANGE, NEW MEXICO	ARD-NM	40,501	122,369.74	302.14		JANUARY 20	2,182	1,652
53	NON-RESIDENTIAL		B-3	218,990	539,882.49	247.10				
54										
55	SOUTHERN UNION GAS COMPANY									
56	SPECIAL SERVICE - SEE NOTE (D)	LOVING, EDDY COUNTY, NEW MEXICO	FS-95	54,647	131,485.49	240.65		FEBRUARY 11	448	330
57										
58	SOUTHERN UNION GAS COMPANY									
59	WELLHEAD SALES - SEE NOTES (D) (H)	EDDY COUNTY, NEW MEXICO	NONE	72,210	51,629.14	71.49		JANUARY 01	629	629 (F)
60										
61	SOUTHERN UNION GAS COMPANY									
62	WELLHEAD SALES - SEE NOTES (D) (H)	SAN JUAN COUNTY, NEW MEXICO	NONE	677,505	1,969,889.95	290.76		FEBRUARY 28	2,809	2,537 (F)
63										
64	SOUTHERN UNION GAS COMPANY									
65	SPECIAL SERVICE - SEE NOTE (D)	FARMINGTON AREA TAPS, NEW MEXICO	X-1	76,821	184,531.04	240.21		MARCH 31	345	295 (F)
66										
67	SOUTHLAND ROYALTY CORPORATION									
68	WELLHEAD SALES - SEE NOTES (D) (H)	SAN JUAN COUNTY, NEW MEXICO	NONE	28,512	71,908.99	252.20		NOVEMBER 15	115	96 (F)

EL PASO NATURAL GAS COMPANY
PAGES 310 AND 311 - SALES FOR RESALE - NATURAL GAS (ACCOUNT 481)
YEAR 1981

LINE NO.	NAME OF OTHER GAS UTILITY (DESIGNATE ASSOCIATED COMPANIES) (A)	POINT OF DELIVERY CITY OR TOWN AND STATE (B)	FERC TARIFF RATE SCHEDULE DESIGNATION (C)	MCF OF GAS SOLD APPROXIMATE BTU PER CU. FT. 1041 (A) (D)	REVENUE FOR YEAR (SEE INSTR. 5) (F)	AVERAGE REVENUE PER MCF (IN CENTS) (F)	SUM OF MONTHLY BILLING DEMANDS (G)	PEAK DAY DELIVERY TO CUSTOMERS DATE (H)	PEAK DAY DELIVERY TO CUSTOMERS MCF NONCOINCIDENTAL (I)	PEAK DAY DELIVERY TO CUSTOMERS MCF COINCIDENTAL (J) (G)
1	NEW MEXICO(CONTINUED)									
2	TENNECO OIL COMPANY									
3	WELLHEAD SALES - SEE NOTES (D) (N)	SAN JUAN COUNTY, NEW MEXICO	NONE	2,018	13,265.18	657.39		JANUARY 31	11	11 (F)
4										
5										
6	TOTAL NEW MEXICO			15,890,644	88,355,793.74					
7										
8										
9	OKLAHOMA									
10	EXPLORATION ASSOCIATES									
11	WELLHEAD SALES - SEE NOTES (D) (N)	DEWEY COUNTY, OKLAHOMA	NONE	265,995	525,697.98	197.67		JANUARY 01	1,801	1,801 (F)
12										
13	R&L OPERATING COMPANY									
14	WELLHEAD SALES - SEE NOTES (D) (N)	WOODWARD COUNTY, OKLAHOMA	NONE	1,239	2,942.84	237.52		MARCH 10	8	8 (F)
15										
16	HRT EXPLORATION									
17	WELLHEAD SALES - SEE NOTES (D) (N)	BECKHAM COUNTY, OKLAHOMA	NONE	326	1,728.57	[illegible]		(E)	0	0
18										
19	MARATHON OIL COMPANY									
20	WELLHEAD SALES - SEE NOTES (D) (N)	HARPER COUNTY, OKLAHOMA	NONE	20	13.55	67.75		(E)	0	0
21										
22	MICHIGAN WISCONSIN PIPE LINE COMPANY									
23	WELLHEAD SALES - SEE NOTES (D) (N)	DEWEY COUNTY, OKLAHOMA	F-1	78,181	51,262.80	65.60		MARCH 19	2,190	0 (F)
24	WELLHEAD SALES - SEE NOTES (D) (N)		F-2	196,799	545,662.07	277.27				
25	WELLHEAD SALES - SEE NOTES (D) (N)		F-3	17,669	7,907.21	44.75				
26	WELLHEAD SALES - SEE NOTES (D) (N)		NONE	35,199	164,165.73	467.06				
27										
28	NATOMAS NORTH AMERICA, INC.									
29	WELLHEAD SALES - SEE NOTES (D) (N)	CADDO COUNTY, OKLAHOMA	NONE	45,384	76,598.68	168.78		JULY 02	291	185 (F)
30										
31	OKLAHOMA GAS AND ELECTRIC COMPANY									
32	WELLHEAD SALES - SEE NOTES (D) (N)	CADDO COUNTY, OKLAHOMA	NONE	6,681	22,763.57	340.72		JANUARY 01	29	29 (F)
33										
34	KIMBROCK GAS COMPANY		NONE		29.13			MAY 01	6	0
35	CD SURCH. DOCKET NOS. CP[illegible]-289 & CP81-312	BEAVER COUNTY, OKLAHOMA-RURAL AREAS	I-1	184	612.16	224.00				
36	SPECIAL SERVICE - SEE NOTE (D)									
37			NONE		361.88			NOVEMBER 01	18	0
38	CD SURCH. DOCKET NOS. CP[illegible]-289 & CP81-312	TEXOLA, BECKHAM COUNTY, OKLAHOMA	I-1	2,769	7,003.58	253.30				
39	SPECIAL SERVICE - SEE NOTE (D)									
40										
41	KIMBROCK GAS COMPANY		NONE		58.95			APRIL 02	13	0
42	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	BEAVER COUNTY, OKLAHOMA	NONE		2.21					
43	RHOD SURCHARGE DOCKET NO. CP76-87		I-1	371	846.98	228.16				
44	SPECIAL SERVICE - SEE NOTE (D)									
45			NONE		267.98			FEBRUARY 02	57	57
46	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	BECKHAM COUNTY, OKLAHOMA	NONE		18.21					
47	RHOD SURCHARGE DOCKET NO. CP76-87		I-1	2,979	6,985.25	217.70				
48	SPECIAL SERVICE - SEE NOTE (D)									
49										
50	SAMEDAN OIL CORPORATION									
51	WELLHEAD SALES - SEE NOTES (D) (N)	CADDO COUNTY, OKLAHOMA	NONE	16,392	62,929.50	383.90		MAY 05	182	21 (F)
52										
53	SAMSON RESOURCES COMPANY									
54	WELLHEAD SALES - SEE NOTES (D) (N)	CADDO COUNTY, OKLAHOMA	NONE		7,810.38 (J)			(E)	0	0
55										
56										
57	TOTAL OKLAHOMA			670,043	1,488,987.83					
58										
59										
60	TEXAS									
61	AMARILLO OIL COMPANY									
62	WELLHEAD SALES - SEE NOTES (D) (N)	GRAY COUNTY, TEXAS	NONE	48,010	79,632.26	165.85		OCTOBER 31	357	0 (F)
63										
64	ATLANTIC RICHFIELD COMPANY									
65	WELLHEAD SALES - SEE NOTES (D) (N)	SCHLEICHER COUNTY, TEXAS	NONE	71,712	81,200.08	113.24		APRIL 30	570	0 (F)
66										
67	BIG LAKE, CITY OF		NONE		13,630.88			FEBRUARY 11	1,135	692
68	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	BIG LAKE, TEXAS	NONE		191.11					
69	RHOD SURCHARGE DOCKET NO. CP76-87		I-1	105,139	321,096.31	237.30				
70	SPECIAL SERVICE - SEE NOTE (D)									

6a

EL PASO NATURAL GAS COMPANY
PAGES 310 AND 311 - SALES FOR RESALE - NATURAL GAS (ACCOUNT 483)
YEAR 1981

LINE NO.	NAME OF OTHER GAS UTILITY (DESIGNATE ASSOCIATED COMPANIES) (A)	POINT OF DELIVERY CITY OR TOWN AND STATE (B)	FERC TARIFF RATE SCHEDULE DESIGNATION (C)	MCF OF GAS SOLD APPROXIMATE BTU PER CU. FT. 1081 (A) (D)	REVENUE FOR YEAR (SEE INSTR. 5) (E)	AVERAGE REVENUE PER MCF (IN CENTS) (F)	SUM OF MONTHLY BILLING DEMANDS (G)	PEAK DAY DELIVERY TO CUSTOMERS DATE (H)	MCF NONCOINCIDENTAL (I)	MCF COINCIDENTAL (J) (G)
1	TEXAS(CONTINUED)									
2	COTTON PETROLEUM CORPORATION									
3	WELLHEAD SALES - SEE NOTES (D) (H)	OCHILTREE COUNTY, TEXAS	NONE	98	337.54	344.43		JUNE 01	9	0 (P)
4										
5	DEL NORTE NATURAL GAS COMPANY									
6	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	EL PASO COUNTY, TEXAS	NONE		299,377.76			JANUARY 19	27,055	18,977
7	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		10,586.95					
8	RESIDENTIAL		R-3	1,332,573	3,198,681.31	240.04				
9	NON-RESIDENTIAL		R-2	1,090,265	2,617,049.79	240.04				
10										
11	DENVER CITY, CITY OF									
12	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	DENVER CITY, TEXAS	NONE		20,846.45			FEBRUARY 11	1,999	1,283
13	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		685.86					
14	SPECIAL SERVICE - SEE NOTE (D)		X-1	122,715	316,365.63	257.81				
15	CITY OF DENVER CITY, TEXAS		PS-3	96,555	148,367.85	153.66				
16										
17	DUMAS, CITY OF									
18	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	DUMAS, TEXAS	NONE		20,783.33			FEBRUARY 10	5,527	3,067
19	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		1,181.29					
20	SPECIAL SERVICE - SEE NOTE (D)		X-1	277,484	653,695.02	235.58				
21										
22	ODESSA NATURAL CO. - SEE NOTE (H)									
23	WELLHEAD SALES - SEE NOTES (D) (H)	PRODUCED GAS, VARIOUS COUNTIES, TEXAS	NONE	1,927,739	5,115,738.13	265.38		MARCH 31	10,857	8,615
24	WELLHEAD SALES - SEE NOTES (D) (H)		NONE	1,006,173	2,335,581.79	232.13				
25										
26	GOLDSMITH, CITY OF									
27	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	GOLDSMITH, TEXAS	NONE		1,991.92			FEBRUARY 10	189	111
28	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		65.61					
29	SPECIAL SERVICE - SEE NOTE (D)		X-1	20,643	48,795.21	236.38				
30										
31	GOOD HOPE REFINERIES, INC.									
32	WELLHEAD SALES - SEE NOTES (D) (H)	ZAPATA COUNTY, TEXAS	NONE	341,038	269,585.55	79.05		(K)	0	0
33										
34	GRANDFALLS, TOWN OF									
35	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	GRANDFALLS, TEXAS	NONE		3,499.54			JANUARY 17	207	159
36	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		100.11					
37	SPECIAL SERVICE - SEE NOTE (D)		X-1	39,889	83,038.91	238.01				
38										
39	HUBER, J.M., CORP.									
40	WELLHEAD SALES - SEE NOTES (D) (H)	ROBERTS COUNTY, TEXAS	NONE	250	785.67	314.27		OCTOBER 01	7	1 (P)
41										
42	MC LEAN, CITY OF									
43	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	MC LEAN, TEXAS	NONE		3,951.65			FEBRUARY 10	829	496
44	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		172.69					
45	SPECIAL SERVICE - SEE NOTE (D)		X-1	48,758	118,112.52	242.29				
46										
47	MORTON, CITY OF									
48	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	MORTON, TEXAS	NONE		17,693.62			FEBRUARY 10	1,228	786
49	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		488.92					
50	SPECIAL SERVICE - SEE NOTE (D)		X-1	166,239	389,711.98	234.43				
51										
52	NORTH BAILEY GAS FARMERS' CO-OPERATIVE SOCIETY									
53	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	PARMER COUNTY, TEXAS	NONE		4,238.28			JULY 25	347	17
54	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		50.37					
55	SPECIAL SERVICE - SEE NOTE (D)		X-1	29,972	66,575.30	225.89				
56										
57	PIONEER NATURAL GAS COMPANY									
58	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	CASTRO AND RANDALL COUNTIES, TEXAS	NONE		2,192.85			MARCH 31	675	397
59	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		292.82					
60	SPECIAL SERVICE - SEE NOTE (D)		X-1	39,088	83,085.37	212.56				
61										
62	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	ECTOR COUNTY, TEXAS-SHELL BOOSTER STATION	NONE		2,360.19			FEBRUARY 11	862	465
63	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		260.83					
64	SPECIAL SERVICE - SEE NOTE (D)		X-1	42,071	89,426.08	212.56				
65										
66	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	GAINES AND ANDREWS COUNTIES, TEXAS	NONE		30,046.69			MARCH 29	6,230	5,993
67	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		3,317.38					
68	SPECIAL SERVICE - SEE NOTE (D)		X-1	535,057	1,137,317.19	212.56				

FERC FORM NO. 14

EL PASO NATURAL GAS COMPANY
PAGES 310 AND 311 - SALES FOR RESALE - NATURAL GAS (ACCOUNT 483)
YEAR 1981

LINE NO.	NAME OF OTHER GAS UTILITY (DESIGNATE ASSOCIATED COMPANIES) (A)	POINT OF DELIVERY CITY OR TOWN AND STATE (B)	FERC TARIFF RATE SCHEDULE DESIGNATION (C)	MCF OF GAS SOLD APPROXIMATE BTU PER CU. FT. 1981 (A) (D)	REVENUE FOR YEAR (SEE INSTR. 5) (E)	AVERAGE REVENUE PER MCF (IN CENTS) (F)	SUM OF MONTHLY BILLING DEMANDS (G)	PEAK DAY DELIVERY TO CUSTOMERS DATE (H)	MCF NONCOINCIDENTAL (I)	MCF COINCIDENTAL (J) (G)
1	TEXAS(CONTINUED)									
2	PIONEER NATURAL GAS COMPANY(CONTINUED)									
3	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	ODESSA, TEXAS	NONE		83.93			FEBRUARY 11	12	9
4	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		4.92					
5	SPECIAL SERVICE - SEE NOTE (D)		I-1	785	1,668.62	212.56				
6										
7	WELLHEAD SALES - SEE NOTES (D) (H)	GRAY COUNTY, TEXAS	NONE	39,798	38,848.68	97.75		FEBRUARY 28	818	815 (F)
8										
9	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	WHARTON COUNTY, TEXAS	NONE		393.48			JANUARY 29	92	91
10	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		37.98					
11	SPECIAL SERVICE - SEE NOTE (D)		I-1	6,173	13,015.04	212.56				
12										
13	PLAINS, CITY OF									
14	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	PLAINS, TEXAS	NONE		8,298.20			FEBRUARY 11	671	469
15	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		262.15					
16	SPECIAL SERVICE - SEE NOTE (D)		I-1	83,489	195,881.38	234.75				
17										
18	RANGAS COMPANY									
19	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	STERLING CITY, TEXAS	NONE		8,779.39			DECEMBER 01	799	275
20	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		136.68					
21	SPECIAL SERVICE - SEE NOTE (D)		I-1	30,092	77,246.43	257.87				
22	RANGAS COMPANY		P3-32	17,779	27,319.88	153.66				
23										
24	RANKIN, CITY OF									
25	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	RANKIN, TEXAS	NONE		6,135.85			NOVEMBER 13	617	292
26	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		197.86					
27	SPECIAL SERVICE - SEE NOTE (D)		I-6	64,193	152,386.84	237.33				
28										
29	RINCROCK GAS COMPANY									
30	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	COLLINGSWORTH COUNTY, TEXAS	NONE		1,669.93			AUGUST 01	96	21
31	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		13.82					
32	SPECIAL SERVICE - SEE NOTE (D)		I-1	9,237	21,937.33	237.49				
33	SPECIAL SERVICE - SEE NOTE (D)		I-19	3,107	6,766.77	217.79				
34										
35	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	COLLINGSWORTH COUNTY, TEXAS	NONE		1,176.06			JULY 31	53	5
36	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		11.78					
37	SPECIAL SERVICE - SEE NOTE (D)		I-1	7,897	17,853.03	226.07				
38										
39	SOUTHERN UNION GAS COMPANY									
40	GENERAL DISTRIBUTION SYSTEM	HOLLY CITY, TEXAS	ARD-TX	12,580	37,869.53	301.09		APRIL 03	10,213	968
41	RESIDENTIAL		A-3	885,107-	2,237,331.53-	252.78				
42	NON-RESIDENTIAL		B-2	1,838,898	3,573,240.54	299.09				
43										
44	GENERAL DISTRIBUTION SYSTEM	EL PASO AND FORT BLISS, TEXAS	ARC-TX	1,717,071	5,185,382.78	301.99		JANUARY 17	109,723	89,204
45	RESIDENTIAL		A-3	4,832,673	11,788,826.71	243.94				
46	NON-RESIDENTIAL		B-2	8,313,712	18,795,126.68	299.09				
47										
48	SPECIAL SERVICE - SEE NOTE (D)	FARWELL, TEXAS	I-1	120,568	287,443.88	238.41		SEPTEMBER 25	681	399
49										
50	GENERAL DISTRIBUTION SYSTEM	LA TUNA, TEXAS	ARD-TX	53,598	161,860.58	301.99		JANUARY 13	2,602	2,083
51	RESIDENTIAL		A-3	198,856	490,463.49	246.15				
52	NON-RESIDENTIAL		B-2	308,062	767,382.15	249.10				
53										
54	GENERAL DISTRIBUTION SYSTEM	SIGNAL PEAK FARM AREA, HUDSPETH COUNTY, TEXAS	ARD-TX	328	990.56	302.00		JUNE 01	95	21
55	RESIDENTIAL		A-3	4,519	10,979.95	242.86				
56										
57	SOUTHERN UNION GAS COMPANY									
58	SPECIAL SERVICE - SEE NOTE (D)	CRANE, TEXAS	I-1	139,523	332,609.56	238.39		FEBRUARY 11	1,298	715
59										
60	SPECIAL SERVICE - SEE NOTE (D)	MENAHARS, TEXAS	I-1	15,596	36,175.02	231.95		JANUARY 16	357	99
61										
62	SOUTHERN UNION GAS COMPANY									
63	SPECIAL SERVICE - SEE NOTE (D)	EDDY COUNTY, NEW MEXICO	I-25	511,891	1,207,968.87	235.98		FEBRUARY 10	6,663	3,510
64										
65	SPUR, CITY OF									
66	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	SPUR, TEXAS	NONE		5,799.39			FEBRUARY 04	573	268
67	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		165.81					
68	SPECIAL SERVICE - SEE NOTE (D)		I-1	55,289	132,118.05	239.36				

313-15

EL PASO NATURAL GAS COMPANY
PAGES 310 AND 311 - SALES FOR RESALE - NATURAL GAS (ACCOUNT 483)
YEAR 1981

LINE NO.	NAME OF OTHER GAS UTILITY (DESIGNATE ASSOCIATED COMPANIES) (A)	POINT OF DELIVERY CITY OR TOWN AND STATE (B)	FERC TARIFF RATE SCHEDULE DESIGNATION (C)	MCF OF GAS SOLD APPROXIMATE BTU PER CU. FT. 1081 (A) (D)	REVENUE FOR YEAR (SEE INSTR. 5) (E)	AVERAGE REVENUE PER MCF (IN CENTS) (F)	SUM OF MONTHLY BILLING DEMANDS (G)	PEAK DAY DELIVERY TO CUSTOMERS: DATE (H)	MCF NONCOINCIDENTAL (I)	MCF COINCIDENTAL (J) (G)
1	TEXAS(CONTINUED)									
2	TROPORO OIL & GAS CO.									
3	WELLHEAD SALES - SEE NOTES (D) (H)	SCHLEICHER, TEXAS	NONE	2,674	7,844.87	293.38		(K)	0	0
4										
5	TRI-COUNTY GAS CO., INC.									
6	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	RURAL AREAS OF BAILEY AND LAMB COUNTIES, TEXAS	NONE		19,626.95			JUNE 24	1,481	85
7	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		287.45					
8	SPECIAL SERVICE - SEE NOTE (D)		X-1	142,058	319,180.00	224.68				
9										
10	UNION TEXAS PETROLEUM									
11	WELLHEAD SALES - SEE NOTES (D) (H)	GLASSCOCK, REAGAN, & UPTON COUNTIES, TEXAS	NONE	151,000	291,958.52	193.35		AUGUST 02	662	319 (F)
12										
13	VAUGHAN WELL CORPORATION									
14	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	WHEELER COUNTY, TEXAS	NONE		7,418.92			FEBRUARY 01	705	678
15	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		342.96					
16	SPECIAL SERVICE - SEE NOTE (D)		X-1	93,973	229,461.08	240.13				
17										
18	WARREC PIPE LINE, INC.									
19	SPECIAL SERVICE - SEE NOTE (D)	WARD AND PECOS COUNTIES, TEXAS	X-1	3,796	8,858.55	233.37		APRIL 07	20	8
20										
21	WESTERN GAS INTERSTATE COMPANY									
22	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	ANTHONY, TEXAS	NONE		951.78			JANUARY 19	70	60
23	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		28.01					
24	GENERAL DISTRIBUTION SYSTEM		ABD-TX	1,730	5,229.29	301.98				
25	RESIDENTIAL		A-3	3,493	9,311.66	266.58				
26	NON-RESIDENTIAL		B-2	5,137	12,815.29	249.47				
27										
28	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	CANUTILLO, TEXAS	NONE		23,260.63			JANUARY 20	1,908	1,502
29	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		712.28					
30	GENERAL DISTRIBUTION SYSTEM		ABD-TX	35,867	108,319.77	301.99				
31	RESIDENTIAL		A-3	178,921	443,599.85	247.93				
32	NON-RESIDENTIAL		B-2	24,998	62,237.00	249.47				
33										
34	WESTAR TRANSMISSION COMPANY									
35	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	CASTRO AND RANDALL COUNTIES, TEXAS	NONE		23,293.37			JULY 23	1,604	0
36	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		219.91					
37	SPECIAL SERVICE - SEE NOTE (D)		X-1	153,191	353,637.21	230.85				
38										
39	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	ECTOR COUNTY, TEXAS-SHELL BOOSTER STATION	NONE		9,216.22			DECEMBER 17	781	0
40	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		48.51					
41	SPECIAL SERVICE - SEE NOTE (D)		X-1	70,773	179,196.28	253.20				
42										
43	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	GAINES AND ANDREWS COUNTIES, TEXAS	NONE		217,023.32			JULY 24	6,625	0
44	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		1,138.68					
45	SPECIAL SERVICE - SEE NOTE (D)		X-1	1,546,925	3,757,258.25	242.89				
46										
47	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	ODESSA, TEXAS	NONE		235.15			AUGUST 31	15	0
48	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		2.02					
49	SPECIAL SERVICE - SEE NOTE (D)		X-1	1,669	4,048.07	242.54				
50										
51	WELLHEAD SALES - SEE NOTES (D) (H)	GRAY COUNTY, TEXAS	NONE	66,854	57,179.71	85.53		MAY 31	715	0 (F)
52										
53	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	YOAKUM COUNTY, TEXAS	NONE		7,946.12			JULY 31	608	0
54	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		13.23					
55	SPECIAL SERVICE - SEE NOTE (D)		X-1	52,862	122,967.19	232.62				
56										
57	WEST TEXAS GAS, INC.									
58	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	COCHRAN AND HOCKLEY COUNTIES, TEXAS	NONE		31,093.15			APRIL 20	3,398	362
59	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		788.57					
60	SPECIAL SERVICE - SEE NOTE (D)		X-1	190,865	445,734.11	233.53				
61	WEST TEXAS GAS, INC.		FS-7	45,716	70,247.88	153.66				
62										
63	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	COCHRAN COUNTY, TEXAS	NONE		578.97			MAY 27	84	11
64	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		13.32					
65	SPECIAL SERVICE - SEE NOTE (D)		A-1	4,272	9,588.72	224.46				
66										
67	CD SURCH. DOCKET NOS. CP77-209 & CP81-312	DUMAS LINE TAPS, TEXAS	NONE		2,048.85			MAY 01	118	7
68	RRQD SURCHARGE DOCKET NO. CP76-87		NONE		25.66					
69	SPECIAL SERVICE - SEE NOTE (D)		X-1	14,302	32,541.73	227.53				

EL PASO NATURAL GAS COMPANY
PAGES 310 AND 311 - SALES FOR RESALE - NATURAL GAS (ACCOUNT 483)
YEAR 1981

LINE NO.	NAME OF OTHER GAS UTILITY (DESIGNATE ASSOCIATED COMPANIES) (A)	POINT OF DELIVERY CITY OR TOWN AND STATE (B)	FERC TARIFF RATE SCHEDULE DESIGNATION (C)	MCF OF GAS SOLD APPROXIMATE BTU PER CU. FT. 1041 (A) (D)	REVENUE FOR YEAR (SEE INSTR. 5) (E)	AVERAGE REVENUE PER MCF (IN CENTS) (F)	SUM OF MONTHLY BILLING DEMANDS (G)	PEAK DAY DELIVERY TO CUSTOMERS DATE (H)	NONCOINCIDENTAL MCF (I)	COINCIDENTAL MCF (J) .5)
1	TEXAS(CONTINUED)									
2	WEST TEXAS GAS, INC.(CONTINUED)									
3	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	GAINES COUNTY, TEXAS	NONE		1,968.12			JULY 10	160	11
4	RHOD SURCHARGE DOCKET NO. CP76-87		NONE		18.20					
5	SPECIAL SERVICE - SEE NOTE (D)		X-1	13,389	30,361.03	226.76				
6										
7	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	GAINES COUNTY, TEXAS-RURAL AREAS OF	NONE		3,718.76			JULY 01	295	113
8	RHOD SURCHARGE DOCKET NO. CP76-87		NONE		76.23					
9	SPECIAL SERVICE - SEE NOTE (D)		X-1	29,986	66,111.30	220.47				
10										
11	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	KERMIT, TEXAS	NONE		27,139.96			FEBRUARY 11	2,926	1,504
12	RHOD SURCHARGE DOCKET NO. CP76-87		NONE		887.90					
13	SPECIAL SERVICE - SEE NOTE (D)		X-1	287,398	685,271.06	238.44				
14										
15	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	M/L TAPS, CULBERSON COUNTY, TEXAS	NONE		41.53			JANUARY 01	2	2
16	RHOD SURCHARGE DOCKET NO. CP76-87		NONE		1.20					
17	SPECIAL SERVICE - SEE NOTE (D)		X-1	360	837.58	232.65				
18										
19	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	SONORA, TEXAS	NONE		8.08			JANUARY 02	1	1
20	RHOD SURCHARGE DOCKET NO. CP76-87		NONE		.39					
21	SPECIAL SERVICE - SEE NOTE (D)		X-1	48	106.89	222.69				
22										
23	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	TOAKUM COUNTY, TEXAS	NONE		727.41			AUGUST 03	40	5
24	RHOD SURCHARGE DOCKET NO. CP76-87		NONE		12.08					
25	SPECIAL SERVICE - SEE NOTE (D)		X-1	5,278	11,987.79	227.13				
26										
27	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	TOAKUM COUNTY, TEXAS-WEST END METER STATION	NONE		11,325.34			JULY 27	929	220
28	RHOD SURCHARGE DOCKET NO. CP76-87		NONE		210.93					
29	SPECIAL SERVICE - SEE NOTE (D)		X-1	92,258	216,202.90	234.35				
30										
31	WHITEFACE, CITY OF									
32	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	WHITEFACE, TEXAS	NONE		4,173.05			JANUARY 17	226	192
33	RHOD SURCHARGE DOCKET NO. CP76-87		NONE		125.64					
34	SPECIAL SERVICE - SEE NOTE (D)		X-1	40,822	96,892.89	237.35				
35										
36										
37	TOTAL TEXAS			23,720,960	58,677,768.39					
38										
39										
40	UTAH									
41	CONSOLIDATED OIL AND GAS COMPANY									
42	WELLHEAD SALES - SEE NOTES (D) (H)	UINTAH COUNTY, UTAH	NONE	1,157	122.92- (J)	10.62-		MARCH 03	22	0 (F)
43										
44	NAVAJO TRIBAL UTILITY AUTHORITY, THE									
45	CD SURCH. DOCKET NOS. CP77-289 & CP81-312	ANETH SCHOOL, SAN JUAN COUNTY, UTAH	NONE		193,065.39			FEBRUARY 11	59	50
46	RHOD SURCHARGE DOCKET NO. CP76-87		NONE		2,285.22					
47	SPECIAL SERVICE - SEE NOTE (D)		X-1	6,991	16,420.24	234.88				
48										
49	SPECIAL SERVICE - SEE NOTE (D)	MONTEZUMA SCHOOL, SAN JUAN COUNTY, UTAH	X-1	8,930	21,195.99	236.80		FEBRUARY 09	50	43
50										
51										
52	TOTAL UTAH			17,078	182,753.92					
53										
54										
55	TOTAL SALES FOR RESALE - NATURAL GAS			1,192,048,089	3,050,933,318.64					
56										

EL PASO NATURAL GAS COMPANY
PAGES 310 AND 311 - SALES FOR RESALE - NATURAL GAS (ACCOUNT 483)
YEAR 1981

LINE NO.	NAME OF OTHER GAS UTILITY (DESIGNATE ASSOCIATED COMPANIES) (A)	POINT OF DELIVERY CITY OF TOWN AND STATE (B)	FERC TARIFF RATE SCHEDULE DESIGNATION (C)	MCF OF GAS SOLD APPROXIMATE BTU PER CU. FT. 1041 (A) (D)	REVENUE FOR YEAR (SEE INSTR. 5) (E)	AVERAGE REVENUE PER MCF (IN CENTS) (F)	SUM OF MONTHLY BILLING DEMANDS (G)	PEAK DAY DELIVERY TO CUSTOMERS DATE (H)	NONCOINCIDENTAL MCF (I)	COINCIDENTAL MCF (J) (G)
1	SUMMARY									
2	A. Field Sales									
3	1. Deliveries to Interstate Pipeline Companies			615,880	1,446,925					
4	2. Others			12,568,623	29,594,036					
5										
6	Total Field Sales			13,184,503	31,040,961					
7										
8	B. Transmission System Sales									
9	1. Interstate Pipeline Companies			80,160,449	208,695,530					
10	2. Intrastate Pipeline Companies and Gas Utilities for Resale			1,098,703,117	2,811,196,824					
11										
12	Total Transmission System Sales			1,178,863,566	3,019,892,354					
13					3,050,933,315					
14										
15					(141,744,032)	(I)				
16	Revenue Adjustment									
17										
18	TOTAL SALES FOR RESALE			1,192,048,069	2,909,189,283					
19										
20										
21										

(A) System-wide weighted average heating value on a pressure base of 14.73 psia at 60° F. saturated.
(B) Yearly weighted average heating value of 1051 BTU at 14.73 psia at 60° F. wet for gas delivered at Topock.
(C) Yearly weighted average heating value at 14.73 psia at 60° F. wet for gas delivered at the following points: Topock, 1051 BTU; Ehrenberg, 1024 BTU.
(D) No service classification reported by purchaser.
(E) Sales other than firm.
(F) Peak day not ascertainable. The metering period in which the highest daily average occurred is shown in lieu of peak day and the peak day volume is assumed to be the average daily delivery in that metering period.
(G) Date of system peak day coincidental delivery is January 31, 1981.
(H) Respondent's leasehold interest in gas disposed of at the well operator's discretion.
(I) Reflects the effect on 1981 gas sales of settlement agreements approved by the FERC at Docket No. RP79-12 covering gas sales rates for the period covered by this report.
(J) Adjustment for prior year.
(K) Peak day not ascertainable.
(L) Clay Basin Surcharge - Revenue attributable to surcharge applicable to Clay Basin Storage Project at Docket Nos. CP77-289 and CP81-312.
(M) Rhodes Reservoir - Revenue attributable to surcharge applicable to Rhodes Storage Project at Docket No. CP76-87.
(N) Associated Company.

Respondent's Brief

1

CORRECTED COPY

Office - Supreme Court, U.S.
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Nos. 81-1889, 81-1958, 81-2042, and 82-19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*, *Petitioners*,

v.

MID LOUISIANA GAS COMPANY, *et al.*, *Respondents*.

On Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

BRIEF OF RESPONDENTS MID LOUISIANA GAS COMPANY, EL PASO NATURAL GAS COMPANY, COLORADO INTERSTATE GAS COMPANY, KENTUCKY WEST VIRGINIA GAS COMPANY, AND KANSAS-NEBRASKA NATURAL GAS COMPANY, INC.

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QUESTION PRESENTED

Whether the court below properly determined that Congress intended the pricing structure of the Natural Gas Policy Act of 1978 to apply equally to all domestic natural gas production, including production by interstate pipelines, intrastate pipelines, and distribution companies, rather than to only the production of independent producers and affiliates of pipelines or distribution companies.

PARTIES BELOW

American Gas Association
Arizona Electric Power Cooperative and City of Wilcox
Ciba-Geigy Corporation
Colorado Interstate Gas Company
Columbia Gas Transmission Corporation
Consolidated Gas Supply Corporation
Ecee, Inc.
El Paso Natural Gas Company
The Federal Energy Regulatory Commission
Kansas-Nebraska Natural Gas Company, Inc.
Kansas State Corporation Commission
Kentucky West Virginia Gas Company
Michigan Wisconsin Pipe Line Company
Mid Louisiana Gas Company
Natural Gas Pipeline Company of America
Northern Natural Gas Company
Northwest Pipeline Corporation
The Public Service Commission of the State of New York
The Public Service Commission of Wisconsin
The State of Michigan and The Public Service Commission of Michigan
Southern Natura Gas Company
United Gas Pipe Line Corporation

LISTING OF AFFILIATES PURSUANT TO RULE 28.1

Mid Louisiana Gas Company ("Mid Louisiana") is a wholly-owned subsidiary of Celeron Corporation (formerly Central Louisiana Energy Corporation). In addition, Mid Louisiana is an affiliate of Celeron Oil and Gas Company (formerly South Louisiana Production Company, Inc.), Louisiana Intrastate Gas Corporation, Trans Louisiana Gas Company, Inc., and LIG Chemical Company.

El Paso Natural Gas Company ("El Paso") is a wholly-owned subsidiary of The El Paso Company. All of El Paso's subsidiaries are wholly-owned, either directly or indirectly, by El Paso. El Paso's affiliates which are not wholly-owned by The El Paso Company, either directly or indirectly, are Geo Nuclear Nobel El Paso and Desert American Insurance Agency, Inc.-Virginia.

Colorado Interstate Gas Company ("CIG") is a wholly-owned subsidiary of Colorado Interstate Corporation, which, in turn, is a wholly-owned subsidiary of the Coastal Corporation. The remaining subsidiaries of The Coastal Corporation and affiliates of CIG are as follows: Coastal Refining Company, Coastal States Petroleum Company, Coastal States Crude Gathering Company, Coastal States Marketing, Inc., CIC Industries, Inc., Derby Refining Company, Pacific Refining Company, Western Fuel Oil Company, Wycon Chemical Company, Coastal Energy Corporation, Coastal Refinery Marketing B.V., Coastal Ventures, Inc., Raffinerie Belge de Petroles S.A. (Belgishe Petroleum Raffinaderij N.V.), Coastal Management Services (Singapore) Pte. Ltd., Coastal States Energy Company, Alaska Petroleum Company, Freeburn Corporation, McCoy-Caney Coal Company, Southern Utah Fuel Company, Utah Fuel Company, Coastal States Management Corporation, Coastal States Trading, Inc., CIG Exploration, Inc., Cosbel Petroleum Corporation, The Belcher Company of New York, Inc., Belcher New England, Inc., Belcher New Jersey Inc., Belcher Oil Company, Belcher Towing Company, Manatee Towing Company, Belcher Terminals, Inc., Belcher Oil Company of Pensacola, the Belcher Company of

Alabama, Inc., The Belcher Company of Georgia, Inc., The Belcher Company of Tennessee Inc., The Belcher Company of Texas, Inc., Coscol Petroleum Corporation, Costa Petro, Coastal Libya, Inc,, Coastal Petroleum (Far East) Pte. Ltd., Coscol Marine Corporation, Coskan Shipping Co., Inc., Holborn Oil Company Limited, Holborn Petroleum S.A., Union Oil Trading & Shipping Limited, Bunyan Charterers Ltd., Coastal States Europe Limited, Pomona Shipping Company Limited, Succula Limited, Coastal States Exploration Services Limited, Coastal States Petroleum (U.K.) Limited, Coastal States Trading U.K.) Limited, Woodstock Shipping Company Limited, Subtype Limited, Holborn-Pomona Petroleum Limited, Holborn Oil Trading Limited, Coastal (Bermuda) Limited, Geogas Enterprise S.A., Sequoia Tankers, Inc., Stonehurst Limited, Texas Tank Ship Agency, Inc., Texcol Gas Services, Inc., Coastal Oil & Gas Corporation, Border Exploration Company, Coastal Congo Exploration Limited, Coastal Indonesia, Inc., Coastal Libya Exploration Limited, Coastal Papua New Guinea Exploration, Inc., Coastal Uranium, Inc., Syrian American Oil Corporation (Texas), Western Enterprises, Inc., CLU Enterprises, Inc., Coastal Christi, Inc., Coastal Hercules, Inc., Coastal Capital Corporation, Coastal Finance Corporation, Coastal Overseas Finance Ltd., Coastal Netherlands Financial B.V., Coastal Financial B.V., Coastal Financial Antilles, N.V., Coastal Offshore Insurance, Ltd., Colbourne Insurance Company Limited, Coastal Limited Ventures Inc., Coastal 1981 Development Program, Ltd., Coastal 1982 Drilling Program, Ltd., CIG Gas Supply Company, Wyoming Gas Supply, Inc., Coastal Coal Sales Company, Overthrust Pipeline Company, Wyoming Interstate Company, Ltd., Petroles D'Outre Mer S.A., Jayhawk Pipeline Corporation, CIG Overthrust Inc., CIG-Canyon Compression, and Canyon Creek Compression Company.

Kentucky West Virginia Gas Company ("Kentucky West") is a wholly-owned subsidiary of Equitable Gas Company, and is an affiliate of Berea Gathering Company, Equitable Gas Energy Company, and Philadelphia Oil Company. In addition, Ken-

tucky West owns 100% of the common stock of Kepco, Inc. and Kentucky Hydrocarbon Company.

The following companies are wholly-owned subsidiaries of Kansas-Nebraska Natural Gas Company, ("Kansas-Nebraska"): Cap-Con International, Inc., Excelsior Oil Corporation, Kan-Col Company of Kansas, Midlands Gas Corporation, Midlands Transportation Company, North Central Energy Company, Northern Gas Company, Northern Mountain Gas Company, Northern Utilities Inc., Slurco, Inc., Western Alfala Corporation, Western Alfalfa Transportation Systems, Inc., Western Gas Corporation, and Wyoming Fuel Company.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
PARTIES BELOW	ii
LISTING OF AFFILIATES PURSUANT TO RULE 28.1	iii
TABLE OF CONTENTS	vi
TABLE OF AUTHORITIES	viii
STATUTES INVOLVED	2
STATEMENT OF THE CASE	3
I. Regulatory Background	4
II. The Natural Gas Policy Act of 1978	7
III. Proceedings Before the Commission	8
IV. The Decision Below	11
SUMMARY OF ARGUMENT	12
ARGUMENT	15
I. The Court Below Properly Determined That Congress Intended The Pricing Structure Of The NGPA To Apply To All Natural Gas Production, Including Production By Interstate Pipelines, Intrastate Pipelines, and Distribution Companies	16
A. The Plain Language Of The NGPA Demonstrates That Congress Intended To Treat Production By Pipelines And Distribution Companies On An Equal Basis With Production By Independent Producers And Affiliates	17
B. An Intracorporate Transfer Of Pipeline Production Qualifies As Both A "Sale" And A "First Sale" Under The NGPA	23
C. The Court Of Appeals' Interpretation Is Consistent With The Legislative History Of The NGPA	31
D. According NGPA Treatment To Production By Pipelines And Distributors Promotes The Objectives And Policies Of The Act	35

Table of Contents Continued

Page

E. Congress Did Not Intend To Discriminate Against Interstate Pipelines Because Of Alleged Historical Distinctions Between The Regulation Of Pipeline Production And The Regulation Of Production By Independent Producers 39

II. The Court Below Properly Refused To Defer To An Agency Interpretation Which Was Manifestly Inconsistent With The Language, Legislative History, And Purposes Of The NGPA 42

III. The Decision Below Does Not Encroach Upon State Jurisdiction Over Retail Sales Of Natural Gas ... 43

IV. Petitioners' Contentions Relating To "Windfall Profits" Are Inaccurate And Are Irrelevant To The Proper Construction Of The NGPA 45

CONCLUSION 49

TABLE OF AUTHORITIES

CASES: Page

Adkins v. *Hampton*, 586 F.2d 1070 (5th Cir. 1978) ... 42

American Electric Power Service Corp. v. *F.E.R.C.*, 675 F.2d 1226 (D.C. Cir. 1982), *cert. granted*, 51 U.S.L.W. 3276 (October 12, 1982) 24

American Tobacco Co. v. *Patterson*, No. 80-1199 (April 5, 1982) 41

Batterton v. *Francis*, 432 U.S. 416 (1977) 43

Cabell v. *Markham*, 148 F.2d 737 (2nd Cir. 1945), *aff'd* 326 U.S. 404 (1945) 23

Canadian River Gas Company, 3 F.P.C. 32 (1942) *aff'd sub nom. Colorado Interstate Gas Co.* v. *F.P.C.*, 324 U.S. 581 (1945) 4, 40, 46

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El Paso Natural Gas Company, 13 F.P.C. 421 (1954) . 9

Federal Election Commission v. *Democratic Senatorial Campaign Committee*, 454 U.S. 27 (1981) 15, 43

F.P.C. v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944) 18

Ferguson v. *Strupa*, 372 U.S. 726 (1963) 46

Ford Motor Co. v. *Milhollin*, 444 U.S. 555 (1980) 43

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Table of Authorities Continued

Page

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Rubin v. *United States*, 449 U.S. 424 (1981) 13, 24

Scripps-Howard Radio Inc. v. *F.C.C.*, 316 U.S. 4 (1942) 32

Tcherepnin v. *Knight*, 389 U.S. 332 (1967) 28

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United States v. *American Trucking Ass'n*, 310 U.S. 534 (1940) 16, 22

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Volkswagenwerk v. *Federal Maritime Commission*, 390 U.S. 261 (1968) 43

Watt v. *Alaska*, 451 U.S. 259 (1981) 23

Wisconsin v. *F.P.C.*, 373 U.S. 294 (1963) 5

STATUTES:

Emergency Petroleum Allocation Act of 1973, 15 U.S.C. 751, *et seq.* 27

Section 8, 15 U.S.C. 757 27

Natural Gas Act, 15 U.S.C. 717, *et seq.* ..... *passim*

Section 4, 15 U.S.C. 717c 22, 44

Table of Authorities Continued

Page

Section 5, 15 U.S.C. 717d 22, 44
Natural Gas Policy Act of 1978, 15 U.S.C. (Supp. V) 3301, *et seq.* ..... *passim*
Section 2(20), 15 U.S.C. (Supp. V) 3301(20) ... 2, 23, 25
Section 2(21), 15 U.S.C. (Supp. V) 3301(21) 2, 3, 12, 17, 18, 21, 22, 30, 34, 36
Section 2(21)(A), 15 U.S.C. (Supp. V) 3301(21)(A) 2, 7, 17, 18, 32, 36
Section 2(21)(A)(v), 15 U.S.C. (Supp. V) 3301(21)(A)(v) 2, 38
Section 2(21)(B), 15 U.S.C. (Supp. V) 3301(21)(B) 3, 7, 8, 9, 11, 17, 18, 19
Section 2(27), 15 U.S.C. (Supp. V) 3301(27) 4
Section 101(b)(9), 15 U.S.C. (Supp. V) 3311(b)(9) ... 30
Section 104, 15 U.S.C. (Supp. V) 3314 47
Section 107, 15 U.S.C. (Supp. V) 3317 41
Section 108, 15 U.S.C. (Supp. V) 3318 ..... 41, 47
Section 109, 15 U.S.C. (Supp. V) 3319 25
Section 201, 15 U.S.C. (Supp. V) 3341 8
Section 203(a), 15 U.S.C. (Supp. V) 3343(a) 21
Section 203(b), 15 U.S.C. (Supp. V) 3343(b) 21
Section 203(b)(1), 15 U.S.C. (Supp. V) 3343(b)(1) . 20, 21
Section 203(b)(2), 15 U.S.C. (Supp. V) 3343(b)(2) 13, 17, 20, 21, 22, 34
Section 501, 15 U.S.C. (Supp. V) 3411 .. 8, 15, 26, 30, 38
Section 501(b), 15 U.S.C. (Supp. V) 3411(b) 8
Section 601, 15 U.S.C. (Supp. V) 3431 44
Section 601(a)(2), 15 U.S.C. (Supp. V) 3431(a)(2) . 44, 45
Section 601(b)(1), 15 U.S.C. (Supp. V) 3431(b)(1) ... 44
Section 601(b)(1)(E), 15 U.S.C. (Supp. V) 3431(b)(1)(E) 14, 28, 29, 30, 34
Section 601(c), 15 U.S.C. (Supp. V) 3431(c) 22

Table of Authorities Continued

Page

Section 601(c)(2)(B), 15 U.S.C. (Supp. V) 3431(c)(2)(B) 44
Section 602(a), 15 U.S.C. (Supp. V) 3432(a) 44
Securities Act of 1933, 15 U.S.C. 77a, *et seq.* 24
Section 17(a), 15 U.S.C. 77q(a) 24

REGULATIONS:

10 C.F.R. 212.72 (1977) 27
10 C.F.R. 212.82 (1977) 28
18 C.F.R. 154.38(d)(4) (1980) 27
18 C.F.R. 282. 303(c) (1982) 27

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H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. (1978) 13, 22, 25, 26, 30, 31, 41

H.R. Rep. No. 95-496 (Pt. 4), 95th Cong., 1st Sess. (1977) 34

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124 *Cong. Rec.* 38361 (1978) 31, 42

124 *Cong. Rec.* 38365 (1978) 31

124 *Cong. Rec.* 38367 (1978) 22

Table of Authorities Continued

Page

Interpretation No. 76-4, 6 Energy Mgmt. (CCH) ¶ 56,290 (April 30, 1976) 28

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

Nos. 81-1889, 81-1958, 81-2042, and 82-19

PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK, *et al.*, *Petitioners*,

v.

MID LOUISIANA GAS COMPANY, *et al.*, *Respondents*.

On Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

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BRIEF OF RESPONDENTS MID LOUISIANA GAS COMPANY, EL PASO NATURAL GAS COMPANY, COLORADO INTERSTATE GAS COMPANY, KENTUCKY WEST VIRGINIA GAS COMPANY, AND KANSAS-NEBRASKA NATURAL GAS COMPANY, INC.

Mid Louisiana Gas Company ("Mid Louisiana"), El Paso Natural Gas Company ("El Paso"), Colorado Interstate Gas Company ("CIG"), Kentucky West Virginia Gas Company ("Kentucky West"), and Kansas-Nebraska Natural Gas Company, Inc. ("Kansas-Nebraska"), each of whom is a respondent in these consolidated proceedings, hereby file their joint brief in opposition to the initial briefs of the Public Service Commission of the State of New York ("New York"), Arizona Electric Power Cooperative, Inc. ("AEPCO"), the State of Michigan ("Michigan"), the Federal Energy Regulatory Commission

("Commission"), and those parties who are supporting the petitioners as *amicus curiae*.[1]

STATUTES INVOLVED

This case involves the Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. (Supp. V) 3301, *et seq.*, pertinent portions of which are set forth in Appendix D. Particularly relevant are the definitions of "sale" and "first sale" which are set forth, respectively, in Sections 2(20) and 2(21) of the NGPA, 15 U.S.C. (Supp. V) 3301(20) and (21):

> "Sale. — The term 'sale' means any sale, exchange, or other transfer for value."
>
> * * *
>
> "First sale. —
>
> (A) General rule. — The term 'first sale' means any sale of any volume of natural gas —
>
> (i) to any interstate pipeline or intrastate pipeline;
>
> (ii) to any local distribution company;
>
> (iii) to any person for use by such person;
>
> (iv) which precedes any sale described in clauses (i), (ii), or (iii); and
>
> (v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this chapter.

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[1] Pursuant to Rule 34.2, the pipeline respondents adopt the Commission's citation to the opinions below and its statement of jurisdiction, as required by Rules 34.1(d) and 34.1(e), respectively. In view of the Court's order of November 29, 1982, granting the parties' motion to dispense with the printing of a joint appendix, all appendix citations refer to the appendix to the petition for a writ of certiorari filed in No. 81-1889 on April 12, 1982, by New York, the initial petitioner in these consolidated proceedings.

(B) Certain sales not included. — Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof."

STATEMENT OF THE CASE

This case involves the applicability of the pricing structure established by the Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. (Supp. V) 3301, *et seq.*, to natural gas which is produced by pipelines and distribution companies. In Order No. 58 (App. B-1), the Commission determined that, except in very limited circumstances, pipelines and distribution companies cannot recover the NGPA prices for their own production, because neither the intracorporate transfer of the gas from the wellhead to the company's transmission system, nor the ultimate sale of the gas to downstream customers, constitutes a "first sale" within the meaning of Section 2(21) of the Act, 15 U.S.C. (Supp. V) 3301(21). Under this interpretation, the pricing of gas produced by interstate pipelines would continue to be regulated by the Commission on a cost basis under the Natural Gas Act, 15 U.S.C. 717, *et seq.*, while the pricing of gas produced by intrastate pipelines and distribution companies would be governed by the various states.

On petitions for review filed by several interstate pipeline companies, Order No. 58 was reversed and vacated by the United States Court of Appeals for the Fifth Circuit. The court specifically held that Congress intended the NGPA pricing structure to apply uniformly to *all* natural gas production, without regard to whether the producer is an independent producer, a pipeline, a distributor, or an affiliate of a pipeline or distributor (App. A-15).[2] The court also determined that, for

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[2] An "independent producer" is a producer which is engaged primarily in the production of natural gas, is not affiliated with a pipeline or distributor, and owns no transmission facilities, with the

the purposes of applying the NGPA prices to pipeline production, Congress contemplated that the "first sale" would occur when there is an intracorporate transfer of the gas from the wellhead to the pipeline's transmission system. *Ibid.*

The pipeline respondents submit that the court of appeals' decision is eminently correct and should be sustained, because it is consistent with the language and legislative history of the NGPA, it promotes the overriding policies and objectives of the Act, and it eliminates an unjustifiable discrimination against a small segment of the nation's gas producers. Prior to addressing these matters in detail, however, it is important to review briefly the regulatory history upon which the petitioners rely to support the Commission's exclusionary interpretation of the Act. As will be seen, it was cost-based regulation under the Natural Gas Act which caused, in large part, the severe gas supply shortages of the mid-1970's, and which led, in turn, to the enactment of the NGPA.

I. Regulatory Background

Prior to the NGPA, the pricing of all natural gas produced and sold for resale in interstate commerce was regulated by the Commission under the Natural Gas Act, 15 U.S.C. 717, *et seq.*[3] Initially, all interstate production (whether produced by an independent producer, pipeline, or pipeline affiliate) was priced on an individual cost-of-service basis.[4] By 1960, how-

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exception of gathering lines located in the production fields. An "affiliate," as defined by Section 2(27) of the NGPA, 15 U.S.C. (Supp. V) 3301(27), includes, insofar as relevant to this proceeding, producers that control, are controlled by, or are under common control with, a pipeline or distributor.

[3] As used herein, "Commission" refers, as appropriate, to either the Federal Energy Regulatory Commission or its predecessor, the Federal Power Commission.

[4] Production by interstate pipelines and pipeline affiliates was regulated by the Commission from the inception of the Natural Gas Act in 1938. *Colorado Interstate Gas Co.* v. *F.P.C.*, 324 U.S. 581 (1945).

ever, it became apparent that regulating several thousand independent producers on an individual cost basis was administratively infeasible. As a result, the Commission abandoned the individual cost-of-service approach for independent producers, and began regulating such sales through the establishment of uniform cost-based rates for all producers within certain geographical areas. *See Wisconsin* v. *F.P.C.*, 373 U.S. 294 (1963); *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968). Subsequently, the Commission further simplified its regulation of independent producers by shifting from area rates to nationwide rates.[5]

The methodology used by the Commission in the establishment of area and nationwide rates, like that historically used in individual cost-of-service ratemaking, was designed to provide independent producers with the opportunity to recover all reasonable costs of exploration, development, and production, including the costs of lease acquisitions and "dry holes".[6] Under the area and nationwide approach, however, the rates established by the Commission were based upon average industry-wide costs, rather than individual company costs. This meant that an independent producer would earn a comparatively lower return if its individual unit costs of

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Sales by independent producers, however, were not regulated until after this Court's decision in *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954).

[5] *See* Opinion 699-H, *Just and Reasonable National Rates for Sales of Natural Gas*, 52 F.P.C. 1604 (1974), *aff'd sub nom. Shell Oil Company* v. *F.P.C.*, 520 F.2d 1061 (5th Cir. 1976), *cert. denied*, 426 U.S. 941 (1976); *see also* Opinion No. 770-A, *National Rates For Jurisdictional Sales of Natural Gas*, 56 F.P.C. 2698 (1976), *aff'd sub nom. American Public Gas Association* v. *F.P.C.*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 907 (1978).

[6] *See, e.g., Permian Basin Area Rate Proceeding*, 34 F.P.C. 159, 192 (1965), *aff'd sub nom. Permian Basin Area Rate Cases*, 390 U.S. 747 (1968); *see also* Commission's discussion in Order No. 98 (App. B-24 to B-25).

production were higher than the industry-wide average. Conversely, the independent producer enjoyed the opportunity to earn a comparatively higher return if its unit costs were lower than the average.

In 1964, while the first area rate proceeding for independent producers was still pending, the Commission initiated an investigation to determine whether it should also depart from individual cost-of-service ratemaking in the pricing of production by pipelines and affiliates. As a result of that investigation, the Commission concluded in Opinion No. 568 that treating pipelines and affiliates in parity with independent producers would encourage exploration and development for additional supplies.[7] Accordingly, the Commission ruled that, in the absence of special circumstances warranting different treatment, pipelines and affiliates would receive the applicable area rates for all gas produced from leases acquired after the date of the order (October 7, 1969).

In Opinion No. 699-H, which established the first nationwide rates for independent producers, the Commission expanded its policy by ruling that pipelines and affiliates, like independent producers, could collect the applicable area or nationwide rates for any gas produced from a well drilled on or after January 1, 1973, without regard to the lease acquisition date.[8] In taking this additional step toward parity, the Commission reasoned that the "natural gas shortage requires the best efforts of all persons whether producer, pipeline, or pipeline affiliate to explore for and develop new supplies of gas to satisfy existing unfilled demands."[9]

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[7] Opinion No. 568, *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738 (1969), *aff'd sub nom. City of Chicago* v. *F.P.C.*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972).

[8] Opinion No. 699-H, *supra*, 52 F.P.C. at 1634-1636.

[9] Opinion No. 699-H, *supra*, 52 F.P.C. at 1636.

Thus, with respect to production from any lease acquired after October 7, 1969, or from any well drilled on or after January 1, 1973, complete price parity among interstate pipelines, affiliates, and independent producers was achieved prior to the enactment of the NGPA. At that time, the only gas being regulated by the Commission on an individual cost-of-service basis was production from pre-1973 wells on pre-October 8, 1969 leases, and production qualifying for a special exception to the area and nationwide rates.

II. The Natural Gas Policy Act Of 1978

With the severe gas shortages which plagued the nation during the mid-1970's, it became apparent that the Commission's regulation of natural gas prices under the Natural Gas Act was flawed in at least two major respects. First, since the Natural Gas Act provided for federal regulation of only the interstate market, gas could be sold in the intrastate market at substantially higher prices than those permitted by the Commission. As a result, producers had little or no incentive to make significant long-term dedications of gas to the regulated interstate market. Second, the Commission's historic and entrenched cost-based approach to the pricing of gas sold in interstate commerce had failed to provide sufficient economic incentives for the development of additional gas supplies.

In response to these problems, and to enhance the nation's future energy security, Congress passed the NGPA in November of 1978. Among other things, the Act established a comprehensive and uniform pricing structure for all "first sales" of natural gas. 15 U.S.C. (Supp. V) 3312-3319. A "first sale" was generally defined by Section 2(21)(A) to mean "any sale of any volume of natural gas" to an interstate or intrastate pipeline, a local distribution company, or any end user. 15 U.S.C. (Supp. V) 3301(21)(A). This provision was qualified, however, by Subsection 2(21)(B), which stated that a "first sale"—

> ". . . shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, *unless such sale is attributable to volumes of natural gas produced by*

such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof." 15 U.S.C. 3301(21)(B) (emphasis added).

With this section, Congress insured that the "first sale" ceiling prices would apply to all natural gas production, including pipeline production, but would not apply to *subsequent resales* of that gas by pipelines, distributors, or their affiliates. Thus, Congress preserved—

(1) the right of a pipeline to recover not only the lawful NGPA price for its acquired and company-owned gas production, but also its additional costs for transporting and reselling the gas; and

(2) the right of a distribution company to recover the total delivered cost of its gas supplies, plus its own cost of distributing and reselling the gas within its market area.

In addition to establishing "first sale" ceiling prices for all categories of natural gas production, the NGPA contained incremental pricing provisions which required the Commission to promulgate rules for the pass-through to certain industrial customers of a portion of all "first sale acquisition costs" for gas either produced or otherwise acquired by a pipeline. 15 U.S.C. (Supp. V) 3341, *et seq.* Moreover, Section 501 of the NGPA vested the Commission with general rulemaking authority to administer the Act. 15 U.S.C. (Supp. V) 3411. Included within this delegation was the authority to define various accounting, technical, and trade terms used in the Act, but only to the extent consistent with the definitions set forth by Congress. 15 U.S.C. (Supp. V) 3411(b).

III. Proceedings Before The Commission

On November 14, 1979, the Commission issued Order No. 58 (App. B-1 to B-13), which promulgated final regulations governing the applicability of the NGPA to production by pipelines, distributors, and affiliates. Specifically, the Commission ruled that a sale of natural gas by an interstate pipeline, intrastate pipeline, or distribution company is not "attributable" to volumes produced by such company, within the

meaning of Section 2(21)(B), 15 U.S.C. (Supp. V) 3301(21)(B), and, therefore, is not entitled to the applicable "first sale" price under the NGPA, unless such sale is "*comprised exclusively* of production volumes . . . from identifiable wells, properties, or reservoirs which are owned by such pipeline or distributor" (App. B-12, emphasis added). Under this definition, pipeline production would qualify as a "first sale" in only two situations: (1) where there is an off-system sale at the pipeline's wellhead, and (2) where a downstream sale involves delivery of gas from an identifiable source which has been dedicated by contract to a particular purchaser (App. B-2 to B-4).[10] In contrast, the Commission determined that any sale by a production affiliate, even if wholly-owned and controlled by a pipeline or distributor, *would* be a "first sale" under the NGPA (App. B-12).

The Commission recognized that the vast majority of pipeline production is neither sold at the wellhead, nor contractually dedicated to particular customers, but, instead, is mixed with gas purchased from other sources to form a general system supply which is then used to serve all customers. As a result, the Commission conceded that "most sales [of pipeline production] by interstate pipelines will not qualify as first sales . . ." (App. B-3). Notwithstanding this concession, the Commission stated that it would not accord "first sale" status to pipeline production sold in mixed volumes, even if it were permitted by the NGPA, because, allegedly, such action would create administrative difficulties and conflict with state jurisdiction over retail sales by pipelines and distribution companies (App. B-4 to B-5).

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[10] When the Commission referred in Order No. 58 (App. B-3) to natural gas "dedicate[d] . . . from an identifiable source to a particular purchaser by contract," it was apparently unaware of the finding of its predecessor, the Federal Power Commission, that such dedicatory provisions in interstate natural gas pipeline contracts are "patently unjust, unreasonable and unlawful and contrary to the public interest." *El Paso Natural Gas Co.*, 13 F.P.C. 421, 458 (1954).

Despite its determination in Order No. 58 that pipelines are not entitled to the NGPA rates as a matter of *law*, the Commission, on August 4, 1980, issued Order No. 98 (App. B-14 to B-49), ruling, as an exercise of its perceived *discretion*, that interstate pipelines could collect the NGPA rates for all pipeline production which formerly qualified for the area or nationwide rates (generally, production from post-1973 wells or post-October 7, 1969 leases), provided the applicable NGPA rates do not exceed "the amount paid in comparable sales" between unaffiliated entities (App. B-47). The Commission emphasized, however, that all pipeline production previously subject to individual cost-of-service treatment would continue to be regulated on that basis under the Natural Gas Act (App. B-14 to B-15, B-27).

On October 3, 1980, the Commission issued Order No. 102, which denied rehearing of Order Nos. 58 and 98 (App. B-50 to B-82). In taking this final action, the Commission placed its imprimatur on a scheme of regulation under which the right to receive NGPA prices for initial sales of natural gas is determined by (1) the corporate form of the producer, and (2) the extent to which the gas in question is mixed with gas from other sources.[11]

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[11] Thus, if an interstate pipeline owned gas production *indirectly* through a wholly-owned and controlled affiliate, it could effectively recover the NGPA rates for the production, regardless of whether the gas is mixed with gas purchased by the pipeline from other unaffiliated producers, and even though such gas had previously been priced on an individual cost-of-service basis under the Natural Gas Act. In contrast, if a pipeline owned the gas production properties *directly* through its own corporate organization, and mixed this production with gas purchased from others, it would not be entitled to the NGPA rates. Instead, the pipeline would be limited to whatever rates the Commission deems appropriate under the Natural Gas Act.

IV. The Decision Below

Shortly after the issuance of Order No. 102, several interstate pipeline companies filed petitions for review in the United States Court of Appeals for the Fifth Circuit. Thereafter, on December 23, 1981, the court of appeals issued a unanimous decision (App. A) vacating Order Nos. 58 and 98. Summarizing its decision, the court stated (App. A-15):

> "Relying on the languag purposes and history of the NGPA, we hold that Co.gress clearly intended for any production attributable to an 'interstate pipeline, intrastate pipeline or local distribution company, or any affiliate thereof' to be accorded first sale status under the NGPA and that Congress contemplated that the intracorporate transfer of pipeline production to the pipeline would be treated as the first sale."

In reaching this conclusion, the court of appeals made essentially three findings. First, after a thorough analysis of the NGPA, the court determined that the Commission's exclusionary interpretation of "first sale" was incompatible with the language of the Act, particularly Section 2(21)(B), 15 U.S.C. (Supp. V) 3301(21)(B), which defines a "first sale" as including the sale of volumes attributable to pipeline production (App. A-8 to A-9). Second, the court found that excluding production by pipelines and distributors from the incentive pricing structure of the NGPA would be inconsistent with the two overriding purposes of the Act, namely, (1) encouragement of additional exploration and development, and (2) elimination of the dual interstate and and intrastate market structure (App. A-9). Finally, the court found that the Commission's narrow interpretation of "first sale" was contrary to the legislative history of the Act (App. A-10).

The court emphasized that according "first sale" status to pipeline production would not encroach upon state jurisdiction over retail rates by intrastate pipelines and local distribution companies. This jurisdiction "would remain intact," the court reasoned, the only change being that the retail price established by the states would reflect "the NGPA cost of gas" (App.

A-13). The court also expressed confidence that the Commission had adequate rulemaking authority, as demonstrated by Order No. 98, to overcome any administrative difficulties arising from the fact that intracorporate transfers of pipeline production are not governed by contracts (App. A-14).

In vacating the Commission's orders, the court recognized that an agency's interpretation of a statute it administers is usually entitled to certain deference. In this particular case, however, the court found that comparatively less deference was required because (1) the concept of "first sale" was relatively new to energy regulation, and, therefore, did not bring into play any experience which the Commission had gained in the administration of the Natural Gas Act; (2) the Commission's interpretation had not been longstanding and tacitly accepted by Congress; (3) the Commission admitted that it had no input into the development of the term "first sale"; and (4) the regulations under review were interpretive, rather than legislative, in nature (App. A-5 to A-7). Under these circumstances, the court reasoned that it could not defer to an interpretation "which could challenge the clear meaning of a statute as revealed by its language, purpose and history." (App. A-7).

SUMMARY OF ARGUMENT

Section 2(21) of the NGPA conclusively demonstrates that Congress intended the "first sale" pricing structure to apply to *all* domestic natural gas production, regardless of the corporate form of the producer. Indeed, the only sales excluded from the NGPA's coverage are *subsequent resales* by pipelines, distribution companies, or their affiliates of gas which they did not produce, but which, instead, was acquired in a prior "first sale." As a result, the court of appeals correctly found that "[n]othing in the language . . . in the NGPA suggests any intent to deny NGPA pricing to natural gas just because it is produced by a pipeline." (App. A-8 to A-9).

There is no merit to petitioners' assertion that intracorporate transfers of pipeline production do not qualify as "first sales" under the NGPA, simply because such transfers do not

involve a change of title or possess all of the indicia of a conventional "sale." As the court of appeals recognized, this assertion is refuted by—

(a) the Commission's admission that it has authority to treat intracorporate transfers as both "sales" and "first sales" (App. B-65; Comm. Br. 28, n. 29);

(b) the Commission's decision in Order No. 98 to apply the NGPA "first sale" prices, as a matter of its perceived discretion, to all intracorporate transfers of pipeline production which previously qualified for the area or nationwide rates (App. B-47); and

(c) the Commission's established practice (since October 7, 1969) of treating certain pipeline production as "purchased" gas, and pricing it on the same basis as production by independent producers and affiliates.

Moreover, by expressly providing for the incremental pricing of the "first sale acquisition cost" of "any natural gas produced by any interstate pipeline," 15 U.S.C. (Supp. V) 3343(b)(2), and by vesting the Commission with authority to "establish rules applicable to intracorporate transactions under the first sale definition,"[12] Congress obviously intended that the terms "sale" and "first sale" would embrace intracorporate transfers. Thus, the narrow definition of "sale" advanced by petitioners "not only is cramped but conflicts with the plain meaning of the statute and its purpose as well." *Rubin* v. *United States*, 449 U.S. 424, 431 (1981).

The court of appeals' decision is firmly supported by the legislative history of the NGPA. There is absolutely nothing in the various reports and debates which accompanied the enactment of the NGPA to suggest that Congress intended to discriminate against production by pipelines and distribution companies. To the contrary, the legislative record demonstrates that Congress intended to abandon the archaic scheme

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[12] H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 116 (1978), *reprinted in* 1978 *U.S. Code Cong. & Ad. News* 8983, 9033 (referred to herein as the "joint conference report").

of cost-based producer regulation under the Natural Gas Act, and to replace it with a statutory pricing structure that would be applied uniformly and comprehensively to *all* natural gas production.

The court of appeals' interpretation also promotes the two major objectives of the NGPA, namely, encouragement of exploration and development and elimination of the dual market structure. In contrast, by excluding pipelines from the incentive pricing structure, petitioners' interpretation would not only discourage exploration and development by a vitally important segment of the gas industry, but, in addition, would create a highly complex regulatory mosaic in which the NGPA determines the price for production by independent producers and affiliates; the Commission determines the price for production by interstate pipelines; and the states determine the price for production by intrastate pipelines and distribution companies. Surely, Congress never envisioned such a highly complex and grossly inequitable result.

There is simply no rational basis to provide the NGPA incentive prices to independent producers and affiliates, which, together, produce more than 95% of the nation's gas supply, yet simultaneously deny those incentives to pipelines and distributors. As the court below held, "[i]n achieving the goal of increasing natural gas production, pipeline producers deserve the price encouragement of [the] NGPA no less than other producers." (App. A-9).

Contrary to petitioners' claim, the court of appeals' decision will not permit all pipelines to receive automatically the NGPA ceiling prices for all company-owned production. Section 601(b)(1)(E) of the Act would prohibit pipelines from pricing any company-owned production at levels which "exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline." 15 U.S.C. (Supp. V) 3431(B)(1)(E). Moreover, even if Section 601(b)(1)(E) were construed to be inapplicable to intracorporate transfers, as petitioners contend, the Commission could still promulgate a "comparable sales" standard for such transfers pursuant to its

authority under Section 501 of the Act. 15 U.S.C. (Supp. V) 3411.

While the decision below properly recognizes that the pricing structure of the NGPA is to be applied uniformly to all gas production, it does not encroach upon state jurisdiction over retail sales by pipelines and distributors. As the court of appeals found, that jurisdiction will remain intact, the only change being that the retail price established by the states will reflect "the NGPA cost of gas." (App. A-13).

Finally, there is no merit to the petitioners' claim that the lower court failed to accord sufficient deference to the Commission's interpretation of the NGPA. As this Court recently stated in *Federal Election Commission* v. *Democratic Senatorial Campaign Committee*, 454 U.S. 27, 32 (1981), the courts remain "the final authorities on issues of statutory construction," and they are compelled "to reject administrative constructions . . . that are inconsistent with the statutory mandate or that frustrate the policy that Congress sought to implement." It was in this spirit that the court of appeals rejected the Commission's discriminatory interpretation of the Act. For similar reasons, the decision below should be sustained in its entirety.

ARGUMENT

The petitioners approach this case with full recognition that the Court has authority to affirm the decision below on the grounds relied upon by the court of appeals or on alternative grounds. Accordingly, they present myriad arguments which challenge not only the lower court's determination that the "first sale" of pipeline production occurs when there is an intracorporate transfer of the gas at the wellhead, but also the alternative construction that the "first sale" of pipeline production occurs when the gas is sold downstream from the pipeline's mixed supply. By interweaving these arguments, however, petitioners have added more confusion than clarity to the issues which must be resolved.

To avoid further confusion and to return the case to its proper focus, this brief will concentrate on the rationale of the court of appeals. While we recognize that the Court has authority to sustain the decision below on the basis of the alternative construction, we believe the court of appeals was unquestionably correct in finding that, for purposes of applying the NGPA pricing structure to pipeline production, the "first sale" occurs when there is an intracorporate transfer of the gas at the wellhead. This construction coincides with the Commission's historic treatment of pipeline production, and it is clearly the approach which was contemplated by Congress.

I. The Court Below Properly Determined That Congress Intended The Pricing Structure Of The NGPA To Apply To All Natural Gas Production, Including Production By Interstate Pipelines, Intrastate Pipelines, And Distribution Companies.

The central issue in this case is whether Congress intended the pricing structure of the NGPA to apply to *all* natural gas production, including the production of pipelines and distribution companies, rather than to only the production of independent producers and affiliates. In resolving this issue, the Court must follow the analytical path which has been established in other cases of statutory construction. Specifically, the Court "must begin with the language of the statute itself," *Dawson Chemical Co.* v. *Rohm & Haas*, 448 U.S. 176, 187 (1980), and, "[a]bsent a clearly expressed legislative intention to the contrary, that language must ordinarily be regarded as conclusive." *Consumer Product Safety Commission* v. *GTE Sylvania*, 447 U.S. 102, 108 (1980). Next, assuming the language is not conclusive and dispositive, the Court must examine the legislative history surrounding the enactment of the statute. *United States* v. *Clark*, 454 U.S. 555 (1982). Finally, the Court must interpret the statute in a manner which effectuates, rather than defeats, the underlying policies and objectives of the statute. *United States* v. *American Trucking Ass'n*, 310 U.S. 534, 542-544 (1940).

Examined in this manner, the NGPA provides no support whatsoever for petitioners' claim that Congress intended to discriminate against pipelines and distribution companies in the application of the NGPA pricing structure. A more rational interpretation—and, indeed, the only interpretation which is compatible with the language, legislative history, and purposes of the Act—is that Congress intended the pricing provisions of the NGPA to apply to *all* natural gas production, regardless of the corporate form of the producer.

A. The Plain Language Of The NGPA Demonstrates That Congress Intended To Treat Production By Pipelines And Distributors On An Equal Basis With Production By Independent Producers And Affiliates.

The starting point for determining the meaning of the NGPA is the language of the statute itself. In this connection, the Court should focus primarily upon Section 2(21), 15 U.S.C. (Supp. V) 3301(21), which defines a "first sale" of natural gas, and Section 203(b)(2), 15 U.S.C. (Supp. V) 3343(b)(2), which relates to incremental pricing of the "first sale acquisition costs" of production by interstate pipelines. Considered together, these sections of the NGPA demonstrate beyond question that Congress intended the "first sale" pricing structure to apply to pipeline production.

1. In language which is uncommonly clear and straightforward, Section 2(21) of the NGPA declares that the term "first sale" shall mean "*any* sale of *any* volume of natural gas" to any pipeline, distribution company, or end user. 15 U.S.C. (Supp. V) 3301(21)(A) (emphasis added). The only exception is found in Subsection (B), which provides that:

> ". . . [A 'first sale'] shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, *unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.*" 15 U.S.C. (Supp. V) 3301(21)(B) (emphasis added).

In an effort to persuade the Court that only the Commission has the requisite competence to interpret the NGPA, petitioners suggest that this subsection is clouded with ambiguity. As the court below recognized, however, that is simply not the case. Each clause of Section 2(21) was carefully worded by Congress to guarantee that the NGPA's new pricing regime would apply to all *initial* sales of natural gas, including intra-corporate transfers of pipeline production, yet simultaneously preserve the right of pipelines and distributors to recover their additional costs of doing business when the gas is *resold* to the next downstream customer.

More specifically, by generally declaring in Section 2(21)(A) that the term "first sale" shall mean *any* sale of *any* natural gas to *any* purchaser, Congress manifested its desire to apply the new ceiling prices to all natural gas production, regardless of its source. Without further qualification, however, the ceiling prices might have obstructed the right of pipelines, which purchase gas in "first sales" made by independent producers, to recover their full costs of service, including not only the applicable NGPA price paid for their purchased gas, but also the just and reasonable costs associated with their transportation and resale of the gas. *Cf. F.P.C.* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944). Similarly, unrestricted application of the ceiling prices could have impeded the right of distributors to recover their own non-gas costs. Thus, it became necessary for Congress to provide in the first clause of Section 2(21)(B) that the "first sale" ceiling prices shall not apply to "the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof . . .". 15 U.S.C. (Supp. V) 3301(21)(B).

If Congress had intended to exclude pipeline and distributor production from the NGPA pricing structure, as petitioners contend, it would simply have terminated Section 2(21)(B) at the end of the first clause. Congress did not do so, however, because it recognized that, while pipelines and distributors function primarily as resellers of gas purchased from others, they frequently produce gas from their own properties—and,

in that role, they are no different from independent producers. Thus, Congress added the so-called unless clause to Section 2(21)(B), thereby insuring that pipelines and distributors would be treated on an equal basis with independent producers in the pricing of gas which is attributable to their own production.

In support of their discriminatory interpretation of "first sale," petitioners focus almost exclusively on the first clause of Section 2(21)(B). In the process, however, they eviscerate the meaning of the unless clause. As the court of appeals reasoned (App. A-8):

> "The Commission's interpretation of section 3301(21)(B) would effectively read the second part of this subsection out of the NGPA. By over-stressing the first provision that sales by a pipeline are not first sales, *the Commission would render the unless clause of subsection (B) a nullity*." (emphasis added).

Notwithstanding the court of appeals' finding, petitioners insist that the unless clause would continue to have meaning under their interpretation, because it would still permit the recovery of NGPA prices for off-system sales. While this is theoretically true, the reasoning of the court of appeals remains unassailable, as a practical matter, because the vast bulk of pipeline production is *not* sold off-system, as the Commission freely admits in Order No. 58, but is sold as part of a mixed system supply consisting of both pipeline production and gas purchased from other sources (App. B-3). In fact, some pipelines make *no* off-system sales of pipeline production. Thus, if the unless clause is to be given any practical meaning, it must be interpreted, as the court of appeals reasoned, to permit NGPA prices for all pipeline production.

Petitioners also contend that the term "attributable," as used in Subsection 2(21)(B), means "exclusively comprised of," and, therefore, a pipeline is not entitled to the NGPA prices for the pipeline production component of a *downstream* sale of mixed volumes. While we disagree with this contention, it will suffice to state that the court of appeals' interpretation of "first sale" is perfectly compatible with petitioners' definition of

"attributable." Indeed, the court found that "treating the intracorporate transfer as a first sale would mean that that sale *would be wholly attributable to the pipeline's production.*" (App. A-13, emphasis added).[13]

2. The court of appeals' interpretation of "first sale" is strongly reinforced by the language of the incremental pricing provisions of the NGPA. In defining the costs which are to be passed through to certain industrial customers, Section 203(b)(1) states that the "first sale acquisition cost" of "acquired" gas shall be the "price paid." 15 U.S.C. (Supp. V) 3343(b)(1). Following this general rule, however, is a subsection which deals specifically with "Interstate Pipeline Production," and states:

> "For purposes of this section, in the case of any natural gas *produced by any interstate pipeline* or any affiliate of such pipeline, the *first sale* acquisition cost of *such* natural gas shall be determined in accordance with rules prescribed by the Commission." 15 U.S.C. (Supp. V) 3343(b)(2) (emphasis added).

By referring to the "first sale acquisition cost" of gas "produced by any interstate pipeline," Congress obviously envisioned that pipeline production would be subject to a "first sale" (App. A-11 to A-12). Otherwise, this provision would

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[13] Ironically, after suggesting that respondents "would read into the statute words that were not put there by Congress," the Commission cavalierly asserts that "attributable" does not mean "attributable," but rather "exclusively comprised of." (Comm. Br. at 17-18). Thus, it is argued that the "first sale" prices could never apply to the *portion* of a mixed downstream sale which represents pipeline production, *vis-a-vis* gas purchased from independent producers. While this argument does not contravene the rationale of the decision below, which finds the intracorporate transfer of pipeline production at the wellhead to be a "first sale," it is important to note that the Commission's definition of "attributable" is inconsistent with the plain meaning of the word and the entire thrust of the NGPA.

essentially be meaningless and inoperative.[14] Moreover, as the court of appeals reasoned (App. A-11):

> ". . . [T]he fact that Congress provided that the 'first sale acquisition cost' of pipeline produced gas would, like the first sale price paid to independent producers, be passed along to the pipeline's ultimate customers suggests that both prices were to be treated in a similar manner. Congress contemplated that the first sale acquisition cost for both pipeline and independent production would be treated as the cost of the gas to the pipeline in determining, under the cost-of-service method, the price charged by the pipeline. *The first sale thus appears to refer to the intracorporate transfer.*" (emphasis added).

Notably, the incremental pricing provisions of Section 203(b)(2), like the "first sale" definition of Section 2(21), make no distinction between affiliate production and pipeline production. Thus, Congress clearly envisioned that *both* categories of production would be accorded "first sale" treatment on an equal basis with production by independent producers.

In an attempt to circumvent the clear meaning of Section 203(b)(2), petitioners assert that, if Congress had intended pipeline production to qualify as a "first sale," there would have been no need for a special rule which treats pipeline production separately from other production for which there is a "price paid." As the court below concluded (App. A-12), however, this distinction merely reflects Congress' awareness that, technically, there is no "price paid" for intracorporate transfers. Congress obviously intended for the Commission to

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[14] If, as petitioners contend, pipeline production is not the subject of a "first sale," such production would not qualify for incremental pricing under the NGPA because Section 203(a), 15 U.S.C. (Supp. V) 3343(a), requires incremental pricing of only "first sales" of domestic production, imports of natural gas or LNG, sales by intrastate pipelines to interstate pipelines, or surcharges paid to other interstate pipelines. This would be plainly inconsistent with the clear indications in Section 203(b)(2), 15 U.S.C. (Supp. V) 3343(b)(2), that pipeline production *would* be subject to incremental pricing. *Cf.*, *Colautti* v. *Franklin*, 429 U.S. 379, 392 (1979) ("a statute should be interpreted so as not to render one part inoperative").

apply the NGPA prices as the "cost" to the pipeline of company-owned production just as the Commission had historically applied the area and nationwide rates under the Natural Gas Act to determine the "cost" of such production.

Relying upon a statement by several congressmen that the language of Section 203(b)(2) "is limited in its applicability . . . to Title II," petitioners also contend that this section has no relevance to the definition of "first sale" which is set forth in Title I of the Act. (Comm. Br. 27). When the entire statement is read, however, it is clear that these congressmen were simply emphasizing, for purposes of clarification, that any rule promulgated under that section "must be consistent with the guarantee contained in Title VI that interstate pipelines may pass through all prices that are just and reasonable under Sections 4 and 5 of the Natural Gas Act."[15] There was no suggestion whatsoever that Congress intended for Title II to function in isolation from the other titles of the Act. Indeed, the phrase "first sale acquisition cost" could have no meaning without reference to the definition of "first sale" set forth in Section 2(21) of Title I.

Moreover, as this Court has frequently observed, statutes must always be read and construed as a whole. *United States* v. *American Trucking Assn.*, 310 U.S. 534, 542-43 (1940). Interpreted in this manner, Sections 2(21) and 203(b)(2) demonstrate conclusively that Congress intended to accord "first sale" status to *all* pipeline production.

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[15] 124 *Cong. Rec.* 38367 (1978). *See also* H.R. Conf. Rep. No. 95-1752, *supra* at 124, 1978 *U.S. Code Cong. & Ad. News* at 9041, explaining that the guaranteed passthrough of "first sales" costs in NGPA Section 601(c) "must be consistent with the incremental pricing provisions of Title II" and that "Title II is structured to permit recovery of all costs which a pipeline is entitled to recover."

B. An Intracorporate Transfer Of Pipeline Production Qualifies As Both A "Sale" And A "First Sale" Under The NGPA.

Petitioners and amici assert that an intracorporate transfer cannot be a "first sale" because it does not initially meet the legal requirements of a "sale." Specifically, it is argued that intracorporate transfers do not involve the traditional indicia of a "sale," such as a change of title or a transfer of cash, and, therefore, they do not fall within the conventional definitions of the term which appear in *Black's Law Dictionary* 1391 (5th ed. 1979) and Section 2-106(b) of the *Uniform Commercial Code*.

1. The first flaw in this reasoning is the failure of petitioners to recognize that the term "sale" is not defined narrowly by Section 2(20), but, instead, is defined broadly to include a "sale" *or* an "exchange" *or* any "other transfer for value." 15 U.S.C. (Supp. V) 3301(20). Equally important, petitioners' hypertechnical interpretation of "sale" ignores the context in which the term was used by Congress. As the courts have consistently recognized, "it is one of the surest indexes of a mature and developed jurisprudence not to make a fortress out of the dictionary; but to remember that statutes always have some purpose or object to accomplish, whose sympathetic and imaginative discovery is the surest guide to their meaning." *Cabell* v. *Markham*, 148 F.2d 737, 739, (2d Cir. 1945) (L. Hand, J.), *aff'd*, 326 U.S. 404 (1945), quoted with approval by this Court in *Watt* v. *Alaska*, 451 U.S. 259, 266, n. 9 (1981).

Examined in this fashion, the term "sale," as used in various federal statutes, has frequently been construed to include transactions which did not possess all of the traditional attributes associated with the term.[16] Thus, in *United Gas Improvement Co.* v. *Continental Oil Co.*, *supra*, 381 U.S. at 399-401, this Court reasoned that, while a sale of leases covering proven

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[16] *See, e.g.*, *Gray* v. *Powell*, 314 U.S. 402 (1941) (no transfer of title); *United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392 (1965) (no "sale" of gas under state law); *United States* v. *Gentile*, 530 F.2d 461 (2nd Cir. 1976), *cert. denied*, 426 U.S. 936 (1976) (no

gas reserves might not technically qualify as a "sale of natural gas" under state law, it would be treated as such under the Natural Gas Act, because the sale "accomplished the transfer of large amounts of natural gas to an interstate pipeline company for resale in other States" and, consequently, it was, "in most respects, equivalent to conventional sales of natural gas . . ." *Id.* at 401. Significantly, the court noted that "[a] regulatory statute such as the Natural Gas Act"—or in this case, the NGPA—"would be hamstrung if it were tied down to technical concepts of local law." *Id.* at 400.

Similarly, in *Rubin* v. *United States*, 449 U.S. 424 (1981), this Court determined that a pledge of stock as collateral for a bank loan was not excluded from the definition of a "sale" under Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q (a), simply because there was no transfer of title. In view of the "economic considerations and realities present" in the transaction, the Court ruled that it could not accept an interpretation of "sale" which "not only is cramped but conflicts with the plain meaning of the statute and its purpose as well." *Id.* at 431.

Applying these principles to the immediate case, it is clear that the court of appeals correctly rejected the Commission's exceedingly narrow interpretation of "sale." If the economic and regulatory objectives of the NGPA are to be advanced in

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transfer of title); and *Rubin* v. *United States*, 449 U.S. 424 (1981) (no transfer of title).

See also American Electric Power Service Corp. v. *F.E.R.C.*, 675 F.2d 1226 (D.C. Cir. 1982), *cert. granted on other grounds*, 51 U.S.L.W. 3276 (October 12, 1982), where the court upheld the Commission's "simultaneous transaction" rule, which requires "utilities, at the cogenerator's option, to engage in a 'simultaneous purchase and sale' by which the utility is *deemed to have purchased* all the cogenerated power, even that used by the cogenerator for itself, *and to have sold* to the cogenerator the power the cogenerator uses internally." *Id.* at 1231 (emphasis added). Basing its decision upon economic realities, the court agreed with the Commission that it was "unlikely that Congress intended the narrow definition of 'purchase' and 'sale' " advanced by petitioners. *Id.* at 1237.

the manner that Congress intended, it is imperative that the term "sale" be realistically interpreted to include intracorporate transfers of pipeline production from the wellhead to the pipeline's transmission system.[17]

2. Contrary to the suggestions of petitioners and *amici*, such intracorporate transfers have significant legal and economic implications, and are clearly "transfers for value." To begin with, except where the mineral interests are owned by the pipeline in fee simple, the production of gas usually triggers the obligation of the pipeline lessee to pay royalties, in the form of either cash or a portion of the gas itself ("in kind"), to the lessor.[18] Equally important, when gas is transferred to the pipeline's interstate transmission system, it becomes subject to the full panoply of regulation under the Natural Gas Act, 15 U.S.C. 717, *et seq.*; thereafter, it cannot be transported or sold by the pipeline except as authorized by the Commission. In exchange for this transfer, the pipeline receives the right to be paid the applicable statutory price for the gas. Consequently, there is clearly both a "transfer for value" and a "sale" within the meaning of Section 2(20) of the Act, 15 U.S.C. 3301(20).

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[17] The Commission contends that intracorporate transfers of pipeline production should not be treated as "first sales" under the NGPA because, historically, the Commission has not issued certificates for such sales under the Natural Gas Act. (Comm. Br. 19-20). However, the NGPA and its legislative history demonstrate that Congress intended the "first sale" pricing structure to apply to all natural gas production, including production which was not previously subject to the Commission's certification requirements under the Natural Gas Act. Indeed, in describing certain "first sale" subcategories in Section 109 of the Act, 15 U.S.C. (Supp. V) 3319, the conference report explains that "the conferees do not intend to require that a certificate has been issued with respect to that gas." H.R. Conf. Rep. No. 95-1752, *supra* at 90; 1978 *U.S. Code Cong. & Ad. News* at 9007.

[18] For example, on lands owned or controlled by the United States, royalty is based on a percentage of the value of the gas "production removed or sold from the lease." 30 U.S.C. 226.

3. The legislative history of the NGPA confirms that Congress intended for the terms "sale" and "first sale" to include intracorporate transfers of pipeline production. For example, in describing the Commission's rulemaking authority under Section 501 of the NGPA, 15 U.S.C. (Supp. V) 3411, the joint conference report states that the Commission may "establish rules applicable to *intracorporate transactions under the first sale definition.*"[19] Petitioners argue that this statement merely indicates that the Commission has the discretion to define intracorporate transactions as "first sales," not that it is required to do so. As the court below ruled, however:

> "This comment [in the report] assumes that intracorporate transactions *will* fall within the first sale definition. The decision which Congress committed to the Commission's judgment was whether regulations were necessary to govern those transactions. *The fact that the Commission was permitted to regulate intracorporate transactions under the first sale definition does not imply that Congress did not intend in the first instance for them to be treated as first sales.*" (App. A-12 to A-13) (emphasis added).

4. Petitioners also suggest that there has never been any regulatory focus upon intracorporate transfers of pipeline production (Comm. Br. 38, n.38), and that treating such transfers as "sales" is a novel regulatory doctrine and a judicially created "fictional transaction." (Commission Br. 15; Mich. Br. 38). To the contrary, however, this is precisely what the Commission itself proposed to do, as a matter of discretion, in Order 98. In order to allow pipelines to collect the NGPA prices for gas produced from post-1972 wells or from leases acquired after October 7, 1969, the Commission would, in effect, impute a "sale" or "transfer for value" at the wellhead; i.e., treat the intracorporate transfer of pipeline production as a sale by the

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[19] H.R. Conf. Rep. No. 95-1752, *supra* at 116 (1978); 1978 *U.S. Code Cong. & Ad. News* at 9033 (emphasis added).

pipeline to itself.[20] Moreover, this is precisely what the Commission has done for the past thirteen years in permitting pipelines to value their own production from post-October 7, 1969 leases by reference to the area or nationwide rates established for independent producers. Indeed, prior to Order No. 98, the Commission's regulations relating to the flow-through of a pipeline's "purchased gas cost" stated:

> ". . .*[P]urchased* gas cost represents the cost of wellhead purchases, field line purchases, plant outlet purchases, transmission line purchases, *and pipeline production that qualifies for and is being afforded area or nationwide rate treatment or is otherwise being afforded rate treatment as though the gas were being produced by an independent producer.*" 18 C.F.R. 154.38(d)(4)(note 1)(1980) (emphasis added).

Needless to say, it is fundamentally inconsistent for the Commission to treat intracorporate transfers of pipeline production as "purchased" gas, and simultaneously deny that it is "sold."

Petitioners' assertion that the decision below creates a novel regulatory doctrine is also refuted by prior interpretations of the term "first sale," as used in Section 8 of the Emergency Petroleum Allocation Act of 1973 ("EPAA"), 15 U.S.C. 757. In its regulations relating to the allocation and pricing of crude oil under that act, the Federal Energy Administration ("FEA") interpreted "first sale" to be the:

> ". . . first transfer for value by the producer or royalty owner. With respect to transfers between affiliated en-

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[20] Indeed, the Commission's incremental pricing regulations concerning pipeline production expressly provide that a "first sale acquisition cost shall be *imputed* to gas *produced* by an interstate pipeline which is *acquired* by the interstate pipeline in a *transaction* which is treated as a first sale," and that the "imputed first sale acquisition cost shall be the applicable maximum lawful price under Title I . . . ." 18 C.F.R. 282.303(c) (1982) (emphasis added). Thus, the Commission has essentially conceded that an intracorporate transfer of pipeline production is both a transfer for value and a sale.

> tities, the 'first sale' shall be *imputed* to occur as if in arms-length transactions." 10 C.F.R. 212.72 (1977) (emphasis added).

More importantly, FEA's regulations defined "transactions between afiliated entities" as including transactions "between entities which are part of the same firm." 10 C.F.R. 212.82 (1977). Thus, when an oil refiner made an intracorporate transfer of oil from its own production properties to its refinery, it was entitled to price the production on a "first sale" basis. In permitting this result, FEA reasoned that a contrary rule would result in "arbitrary discrimination between refiners based solely upon technicalities of corporate organization" for which there was "no rational basis whatever." *Interpretation No. 76-4*, 6 Energy Mgmt. (CCH) ¶ 56,290 at p. 56,340 (April 30, 1976).

Similarly, the court below properly refused to define "sale" or "first sale" in a rigid manner which would subvert the intent of Congress. It obviously recognized that remedial legislation must be construed broadly to effectuate its purposes, and, to that end, "form should be disregarded for substance and the emphasis should be on economic reality." *Tcherepnin* v. *Knight*, 389 U.S. 332, 336 (1967).

5. Petitioners rely heavily on the fact that intracorporate transfers of pipeline production are not expressly mentioned in Section 601(b)(1)(E)—the "affiliated entities limitation"—which provides essentially that any amount paid in a first sale "between any interstate pipeline and any affiliate of such pipeline" will be deemed just and reasonable if, among other things, it "does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline." 15 U.S.C. (Supp. V) 3431 (b)(1)(E). As a result of this omission, it is first asserted that pipeline production is not covered by Section 601(b)(1)(E). From this premise, it is then argued that the failure of the NGPA to provide a "comparable sales" standard for pipeline production indicates that Congress did not intend for such production to be accorded "first sale" prices.

In fact, however, Section 601(b)(1)(E) does cover intracorporate transfers of pipeline production. While the language of that section is less than clear, the legislative history readily demonstrates that when Congress referred to "any first sale between any interstate pipeline and any affiliate of such pipeline," 15 U.S.C. (Supp. V) 3431 (b)(1)(E), it sought to embrace *any* transfer of gas—including an intracorporate transfer—which is not made at "arms length."[21] It is thus clear that the "comparable sales" standard of Section 601(b)(1)(E) applies to both affiliate production *and* pipeline production.

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[21] In June 1978, the House and Senate conferees convened to reconcile the House bill (H.R. 8444) and the Senate bill (S. 2104) into the legislation which ultimately became the NGPA. While the House bill contained no "affiliated entities limitation," Sections 205 and 206 of the Senate bill would have amended the Natural Gas Act to preclude the Commission from preventing the pass-through of the NGPA costs, except where the pipeline—

> ". . . purchases new gas from an affiliate *or produces new natural gas from its own properties*, to the extent that the Commission determines that the rates and charges therefor exceed the current rate . . . for comparable sales by persons not affiliated with such natural-gas company." (emphasis added).

In a memorandum containing recommendations for the reconciliation of the House and Senate bills, the Staff of the Senate Committee on Energy and Natural Resources summarized Section 205 and 206 of the Senate bill in language which is strikingly similar to the language ultimately chosen for Section 601(b)(1)(E) of the NGPA. Specifically, the Staff stated that the Senate bill guarantees that interstate pipelines can pass through their NGPA gas costs if the price does not exceed, "in the case of sales *between affiliated entities*, the price received in comparable transactions by persons not affiliated with the pipeline." It is thus clear that, when Congress provided in Section 601(b)(1)(E) for a "comparable sales" limitation on "any first sales *between any interstate pipeline and any affiliate*," it was referring, as the Senate bill had, to both purchases from an affiliate *and* pipeline production. *See* Memorandum dated June 6, 1978, from Senator Henry M. Jackson to Senate Conferees on Natural Gas, pertinent portions of which are appended to the brief of Michigan Wisconsin Pipe Line Company.

Moreover, even if Section 601(b)(1)(E) were construed, as petitioners urge, to apply only to sales by affiliates *to* pipelines, it would not follow that Congress intended to exclude pipeline production from the NGPA.[22] It would simply mean that Congress intended for the Commission to establish appropriate "comparable sales" standards under Section 501, which, according to the joint conference report, provides the Commission with general authority to "establish rules applicable to *intracorporate transactions under the first sale definition.*"[23]

In view of the Commission's authority under Sections 601(b)(1)(E) and 501, there is no merit to petitioners' argument that treating an intracorporate transfer of pipeline production as a "first sale" will automatically entitle pipelines to collect the maximum NGPA ceiling prices, whereas independent producers would be limited under Section 101(b)(9), 15 U.S.C. (Supp. V) 3311 (b)(9), to the terms of their "arm's length" contracts. (Comm. Br. 31-32, 37). The court of appeals did not hold that pipelines have superior rights to independent producers and affiliates under the NGPA. It simply ruled that all provisions of the Act—however conditioned or qualified by Congress—must be applied equally to *all* producers, not just a select majority.

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[22] Section 601(b)(1)(E) was not designed to define "first sale," but rather to limit the value of the gas which can be passed through to the pipeline's customers. Thus, however interpreted, this section cannot negate the express language of Section 2(21) which, as we have shown, clearly defines "first sale" as including sales of volumes attributable to pipeline production.

[23] H.R. Conf. Rep. No. 95-1752, *supra* at 116; 1978 *U.S. Code Cong. & Ad. News* at 9033. In fact, the Commission adopted such a "comparable sales" standard in Order No. 98 with respect to intracorporate transfers of gas produced by pipelines from post-1972 wells or post-October 7, 1969 leases. Specifically, the Commission ruled that an interstate pipeline will be permitted to charge the *lower* of the NGPA rates *or* "the amount paid in comparable sales . . . between persons not affiliated with such interstate pipeline or with each other." (App. B-47).

C. The Court Of Appeals' Interpretation Is Consistent With The Legislative History Of The NGPA.

1. While the legislative history of the NGPA does not specifically elaborate upon the definition of "first sale," it broadly supports the court of appeals' conclusion that Congress intended the new pricing structure to apply to all natural gas production, rather than to only the production of independent and affiliated producers. There is no evidence whatsoever that Congress envisioned a fragmented regulatory structure, in which independent producers and pipeline affiliates would be entitled to the applicable NGPA prices, but the production of interstate pipelines would continue to be regulated by the Commission under the Natural Gas Act. To the contrary, the various committee reports and statements accompanying the NGPA reflect a widespread congressional belief that cost-based regulation under the Natural Gas Act was an "outdated mode of regulation,"[24] and that it should be replaced with a uniform and comprehensive pricing structure which applies to "any"[25] and "all"[26] gas production. Accordingly, the economic analysis of the Act declared:

> "[The NGPA] *alters the present system of cost based controls* on the wellhead price of natural gas sold in interstate commerce to *a statutory price formula applicable to both interstate and intrastate sales* . . . It is apparent that the

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[24] Statement of Rep. Dingell, Chairman of the House Interstate and Foreign Commerce Committee, 124 *Cong. Rec.* 38361 (1978).

[25] H.R. Conf. Rep. No. 95-1752, *supra* at 74; 1978 *U.S. Code Cong. & Ad. News* at 8991. ("The first sale . . . means any sale of any volume of natural gas . . ."). *See also* Chairman Dingell's statement that Section 104 of the NGPA, 15 U.S.C. (Supp. V) 3314, "is not limited to existing contracts and successors to existing contracts but is applicable to any interstate gas for which a just and reasonable rate exists." 124 *Cong. Rec.* 38365 (1978).

[26] H.R. Conf. Rep. No. 95-1752, *supra* at 72; 1978 *U.S. Code Cong. & Ad. News* at 8989. ("The Conferees agreed that *all* natural gas prices would be allowed to escalate with inflation . . .").

present dual market of natural gas pricing, *including cost based regulation of the interstate market, is no longer tenable.*" (emphasis added.)[27]

There is simply no way the Commission's assertion of jurisdiction over pipeline production can be reconciled with these unequivocal declarations of congressional intent.

2. Petitioners readily concede that their interpretation of the NGPA finds no express support in the legislative record,[28] and they acknowledge that congressional silence is frequently an unreliable guide to legislative intent. *Scripps-Howard Radio Inc.* v. *F.C.C.*, 316 U.S. 4, 11 (1942). In this particular case, however, petitioners find meaning in the legislative record's comparative silence on the matter of pipeline production, because, allegedly, Congress would not have changed several decades of Commission regulation of pipeline production, without providing a detailed discussion of its reasons.

The weaknesses in this rationale are manifold. First, to the extent the legislative record's silence on pipeline production is relevant, that silence favors an interpretation which avoids discrimination, on the basis of corporate form, against a particular class of gas producers. In view of the manifest desire of Congress to apply the NGPA pricing structure to "any sale of any volume of natural gas,"[29] with the sole exception of resales by pipelines, distributors, and affiliates, it is completely understandable that Congress did not provide a detailed legislative analysis of the specific category of pipeline production. Indeed,

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[27] House Interstate and Foreign Commerce Committee, Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978, H.R. Pub. No. 95-62, 95th Cong. 2nd Sess. 1-2 (1978).

[28] In its petition for a writ of certiorari, filed with the Court on July 6, 1982, the Commission admitted (p. 20) that "there is no discussion of cost-of-service pricing in the statute or in its legislative history." Similarly, the Commission's brief acknowledges (p. 25) that "there is little discussion in the debates and other relevant legislative sources focusing specifically on pipeline production."

[29] Section 2(21)(A) of the NGPA, 15 U.S.C. 3301(21)(A).

a detailed discussion of pipeline production would be expected only if Congress had intended to exclude this specific category of gas from the general coverage of the statute.

Second, it is undeniable that the legislative record is no more illuminative with respect to the "first sale" treatment of affiliate production than it is with respect to pipeline production. Yet, the Commission readily concedes that affiliates are entitled to the NGPA prices as a matter of law. If the statute is to be interpreted fairly and consistently, pipelines must be accorded the same treatment.

Finally, there is nothing aberrational about a change in the historic method of regulating pipeline production. Indeed, as the Commission recognizes, the NGPA radically changed several decades of cost-based regulation of the prices charged by independent producers and pipeline affiliates, who, together, produce more than ninety-five percent of the nation's gas supply. Under these circumstances, it would be anomalous to conclude that Congress intended to continue the regulation of pipeline production under a structure which was widely perceived as archaic and requiring change.

3. Relying upon various statements in the Committee reports and debates relating to the NGPA, petitioners also argue that Congress intended the pricing structure of the Act to apply only to wellhead sales. As the court of appeals recognized, however, there are two problems with this assertion. (App. A-10). First, it is contrary to the Commission's own determination in Order No. 58 that the downstream sale of pipeline production *is* a "first sale" under the NGPA, to the extent it involves the sale of identifiable volumes which are contractually dedicated to a particular customer. Second, as the court of appeals reasoned, the legislative history equating a "first sale" with a wellhead or field sale simply confirms that, in the context of pipeline production, Congress envisioned that "the intracorporate transfer from the production division of the pipeline to the transportation division of the pipeline would

constitute the first sale." (App. A-10 to A-11).[30] Thus, the decision below is totally compatible with petitioners' assertion that wellhead sales were the primary focus of the NGPA.[31]

In sum, the legislative history of the NGPA, like the language of the Act itself, fully supports the decision below. Congress clearly intended to incorporate all domestic gas production within the pricing structure of the NGPA, and to guarantee that there would be "no indirect or 'back door' producer regulation by FERC."[32]

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[30] Testifying before the House Subcommittee on Energy and Power, Mr. David D. Schwartz, formerly the Assistant Chief of the Office of Economics of the Federal Power Commission, stated without contradiction:

> "There is no doubt that the major interstate pipelines (as well as distributors with producing affiliates) will benefit from the pricing provisions because all of them have producing affiliates *or divisions*." (emphasis added).

Hearings on H.R. 6831, *et al.*, Before the Subcommittee on Energy and Power of the House Committee on Interstate and Foreign Commerce, 95th Cong., 1st Sess., ser. 95-93, Pt. 2 at 893-894 (1977).

[31] Petitioners' attempt to exclude pipeline production from the NGPA pricing structure is not aided by the statement in an earlier Congressional report that the term "first sale" should be applied by the Commission "to the first transfer of natural gas for value in an arms-length transaction." H.R. Rep. No. 95-496 (Pt. 4), 95th Cong., 1st Sess. 103 (1977). To begin with, this report related to an earlier bill, H.R. 6831, which did not define "first sale." In contrast, the NGPA, as enacted, expressly defined "first sale" to include pipeline production, 15 U.S.C. (Supp. V) 3301(21); provided for the incremental pricing of the first sale acquisition cost of pipeline production, 15 U.S.C. (Supp. V) 3344(b)(2); and established an "affiliated entities limitation," 15 U.S.C. (Supp. V) 3431(b)(1)(E). Moreover, the Commission's recognition that sales by affiliates are "first sales" demonstrates that Congress did not intend to limit the NGPA pricing structure to arms-length transactions.

[32] Natural Gas Pricing Agreement Adopted by Conferees as H.R. 5289, 95th Cong., 2d Sess. 19 (Comm. Print No. 95-55, June 1978).

D. According NGPA Treatment To Production By Pipelines And Distribution Companies Promotes The Objectives And Policies Of The Act.

In addition to being consistent with the language and history of the NGPA, the court of appeals' interpretation of "first sale" promotes the two cardinal objectives of the Act, namely, (1) encouragement of additional exploration and development, and (2) the elimination of the dual market structure. In contrast, the petitioners' discriminatory interpretation is inconsistent with both of these goals. First, by depriving pipeline producers of the economic incentives available to independent producers and affiliates, the Commission's rule would discourage exploration and development by a small, yet vitally important, segment of the gas industry. Second, the Commission's exclusion of production by intrastate pipelines and distribution companies would perpetuate, rather than eliminate, the dual market structure, and would thereby leave intact "a substantial vestige of the dual market structure Congress sought to eliminate" (App. A-10). In fact, the Commission's rule would create a tripartite regulatory framework in which independent and affiliated producers would receive the applicable NGPA rates; interstate pipelines would receive rates determined by the Commission under the Natural Gas Act; and intrastate pipelines and distribution companies would receive the rates permitted by the particular states in which their properties are located. As the lower court recognized, Congress never envisioned such a byzantine and fundamentally inequitable result.

1. With respect to the first objective of the NGPA—encouragement of additional exploration and development—the Commission admits that application of the incentive pricing structure to pipeline production would increase the gas supply in the market areas served by the pipelines. In its view, however, this is insignificant, because Congress intended the incentives to apply to independent producers, who provide gas supply to all systems, but not to pipelines, "who are only secondary sources of supply, and then primarily for their own systems." (Comm. Br. 29).

The initial flaw in this argument is its blatant inconsistency with several decades of regulation in which the Commission has constantly recognized that pipeline production should be favored, rather than discouraged, because it maximizes consumer benefits.[33] More importantly, it is absurd to suggest that gas produced by pipelines is less important to the nation's energy balance than gas produced by independent producers. As Congress obviously recognized, natural gas is a fungible commodity; therefore, all additional exploration and development—whether undertaken by an independent producer, a pipeline, or any other producing entity—serves to enhance the nation's energy security. Accordingly, the "first sale" pricing structure of Section 2(21) of the NGPA is not limited to sales by independent producers. It applies to "any sale of any volume of natural gas," with the single exception of resales by pipelines, distribution companies, and affiliates. 15 U.S.C. (Supp. V) 3301(21)(A).

The Commission's argument concerning the alleged "secondary" importance of pipeline production is also fundamentally inconsistent with its treatment of producing affiliates, which are typically wholly-owned and controlled by pipelines, and which function for the primary purpose of providing gas supply to their pipeline affiliate. If affiliate production is entitled to NGPA treatment, notwithstanding the fact that affiliates are not engaged primarily in "arms length" sales to all pipeline systems, then surely the production of the pipelines themselves cannot be disqualified on the

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[33] In *Panhandle Eastern Pipe Line Company*, 13 F.P.C. 53, 74 (1954), *rev'd on other grounds sub nom. City of Detroit* v. *F.P.C.*, 230 F.2d 810 (D.C. Cir. 1954), *cert. denied*, 352 U.S. 829 (1956), the Commission declared that "the interest of the public definitely lies in the direction of natural gas production by pipeline systems themselves, as distinguished from their complete dependence for gas supplies upon purchases from other producers," because, among other things, it "strengthens their bargaining position in negotiating gas-purchase contracts with independent producers . . . ."

ground that it is used primarily to serve only one system's needs.[34] As the court below held, "in achieving the goal of increasing natural gas production, pipeline producers deserve the price encouragement of NGPA no less than other producers." (App. A-9).[35]

2. Petitioners also assert that denying NGPA treatment to pipelines and distribution companies is consistent with the second goal of the NGPA—elimination of the dual market structure. Specifically, it is alleged that pipeline production had "only a marginal impact on the dual market problem," because, unlike independent producers, pipelines were not "shopping in the marketplace" for higher prices, but, instead, were simply seeking to maintain sufficient reserves for their own systems. (Comm. Br. 28-29).

Again, the Commission's view is both myopic and inconsistent with its treatment of pipeline affiliates. Congress did not scrutinize each producer or each segment of the industry to determine the precise impact of that particular producer

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[34] In fact, many interstate pipelines resell substantial volumes of gas downstream to other interstate pipelines. On the other hand, producers and affiliates frequently sell all of their production to a single pipeline.

[35] It is untenable for petitioners to suggest that the Commission's interpretation of the NGPA promotes new exploration and development by interstate pipelines, because the Commission, as an exercise of discretion, has determined in Order No. 98 that pipelines should receive the applicable NGPA rates for any company-owned production which previously qualified for the area or nationwide rates. As the court of appeals recognized (App. A-9):

> "This argument is sophistic. The Commission's duty is to administer the law Congress passed in light of the purposes for which it was passed. It is not an agency's prerogative to alter a statutory scheme even if its alteration is as good or better than the congressional one. *The fact that the agency gives back all or part of what it takes from the law's grant in no way justifies departure from the congressional purpose in the first instance.*" (emphasis added).

or segment on the problems which were being addressed. To the contrary, it sought to establish a single pricing structure that would be applied *uniformly* and *comprehensively* to *all* natural gas production on the basis of well characteristics, without regard to either the corporate form of the producer or the extent to which that particular producer caused the problems for which a solution was sought. Consequently, an independent producer or an affiliate is covered by the NGPA pricing structure, even if, prior to the Act, the company was committing 100% of its supply to the interstate market and was operating at a substantial profit. Under these circumstances, it is untenable for petitioners to claim pipelines must be excluded from the NGPA pricing coverage, because they were only a "marginal" cause of the problems addressed by Congress.

It is likewise untenable for the Commission to suggest that its interpretation is consistent with the goal of eliminating the dual market structure because it retains discretionary authority to deal with the problem under Sections 2(21)(A)(v) and 501 of the NGPA. 15 U.S.C. (Supp. V) 3301(21)(A)(v) and 3411. (Comm. Br. 28; App. B-6 to B-8). That misses the point entirely. The question is not whether the Commission is vested with discretionary authority to eliminate the dichotomy between the interstate and intrastate markets, but whether that dichotomy has been eliminated by congressional mandate. On this point, there can be no doubt. As demonstrated by the legislative history of the NGPA, Congress clearly intended to abandon "the artificial distinction between the interstate and intrastate markets,"[36] and to establish "a statutory price control formula applicable to both interstate and intrastate sales."[37]

In short, the court of appeals was absolutely correct in finding that the two principal objectives of the NGPA—encouragement of additional exploration and development and

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[36] S. Rep. No. 95-436, 95th Cong., 1st Sess. 21 (1977).

[37] House Interstate and Foreign Commerce Committee, Economic Analysis of H.R. 5289, *supra* at 1-2.

elimination of the dual market structure—can be achieved only if all producers are treated on an equal basis.

E. Congress Did Not Intend To Discriminate Against Interstate Pipelines Because Of Alleged Historical Differences Between The Regulation Of Pipeline Production And The Regulation Of Production By Independent Producers.

In order to circumvent the clear meaning of the NGPA, as illuminated by its language and legislative history, petitioners and *amici* suggest that the court below failed to give appropriate weight to alleged historical differences in the Commission's regulation of pipeline producers, *vis-a-vis* independent producers. In this connection, it is asserted that individual cost-of-service regulation provided pipelines with the right to recover all prudently incurred exploration costs, including lease acquisition costs and the costs of "dry holes," and, therefore, pipeline producers were shielded from the risks traditionally borne by independent producers.

The first problem with this contention is its mistaken factual premise that, historically, independent producers were not compensated for their risks. As the Commission has conceded in Order No. 98, the area and nationwide rates established for independent producers were designed "to provide for recovery of the average costs of finding, developing and producing gas *plus* an incentive *to compensate for the risks* associated with lease acquisition, exploration, and development." (App. B-25, emphasis added). Moreover, as the Commission admits in its brief (p. 4, n. 6), the area and nationwide rates specifically included a component to compensate independent producers for "dry hole" costs. Under these circumstances, it is nonsensical for the Commission to attempt to justify its discrimination against pipelines by simply reasoning that pipelines have "passed on the costs of acquiring leases and the costs of exploration and development, including dry hole costs . . ." (App. B-27; Comm. Br. 10). Obviously, the same can be said

about independent producers and affiliates, both of whom have been accorded NGPA treatment.[38]

Secondly, and more importantly, the Commission's argument concerning the significance of its historical treatment of cost-of-service production is refuted by its own rationale in Order No. 58. In that order, the Commission properly determined that any sale of production by an affiliate, *including production formerly regulated on a cost-of-service basis*, is a "first sale" which is entitled to the applicable NGPA rate (App. B-9, B-12 to B-13). The Commission also ruled that a "first sale" includes any sale of identifiable pipeline production, *including production formerly regulated on a cost-of-service basis*, which is contractually dedicated to a particular customer (App. B-3).

In both of these situations—affiliate sales and pipeline sales of identifiable volumes contractually dedicated to a particular customer—the production sold from pre-1973 wells on pre-October 8, 1969 leases would have the *identical* historical attributes as the pipeline production which, according to the Commission, continues to be regulated on a cost-of-service basis. Under these circumstances, it is clear that the Commission's discriminatory treatment of pipeline production is not

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[38] In fact, the methodology historically used by the Commission to calculate the individual cost-of-service for pipeline production was the same, in all material respects, as that used to calculate the area and nationwide rates for independent producers. The only significant difference was that the pipeline's cost-of-service was calculated on the basis of test-year costs and sales volumes for the individual company, whereas the area and nationwide rates were calculated on the basis of average industry-wide costs and production volumes. Notably, however, in many situations, the *actual* per unit costs subsequently incurred by the pipeline producer exceeded the *test-year* unit costs upon which its cost-of-service rates were based, thereby effectively lowering the pipeline producer's return. *See Colorado Interstate Gas Co.* v. *F.P.C.*, 324 U.S. 581, 608-615 (1945) (Jackson, J., concurring opinion). In short, petitioners and *amici* are flatly wrong in describing pipeline production as a risk-free operation.

based upon legitimate historical differences, but upon (1) the corporate *form* of the producer, and (2) the fact that most pipeline production is mixed with purchased gas prior to sale. Neither of these facts, however, can justify the Commission's interpretation of the Act. As this Court recently emphasized, statutes must be interpreted "to avoid untenable distinctions and unreasonable results whenever possible." *American Tobacco Co.* v. *Patterson*, No. 80-1199 (April 5, 1982), slip op. at 8.

Finally, to the extent there have been any historical differences in the regulation of certain classes or vintages of gas, such differences would not provide a rational basis for concluding that Congress intended to exclude pipeline production from the unified pricing structure of the NGPA. Pipeline producers of Devonian shale gas, for example, which is governed by Section 107, 15 U.S.C. (Supp. V) 3317, or "stripper" well gas, which is governed by Section 108, 15 U.S.C. (Supp. V) 3318, are just as entitled as independent producers and affiliates to receive the NGPA incentive prices. Yet, under the petitioners' construction, gas produced from the same field—and, in some cases, the same well—would be subject to vastly different prices, depending on the corporate form of the producer.[39] There is simply no basis upon which this construction can be

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[39] The absurd result of the Commission's interpretation is demonstrated by considering a situation in which an interstate pipeline, an affiliate of an interstate pipeline, and an intrastate pipeline share equally in the production from a *single* well. According to the Commission, the *same* gas produced from this single well could be priced at three different levels under three separate legal regimes: the Commission would establish a rate under the Natural Gas Act for the interstate pipeline's share of the production; the NGPA would govern the rate for the affiliate's share; and the state would determine the rate for the intrastate pipeline's share. This kind of "patchwork" pricing is totally imcompatible with the manifest intent of Congress to establish "*a single uniform price policy* for natural gas produced in the United States." H.R. Conf. Rep. No. 95-1752, *supra* at 67; 1978 *U.S. Code & Ad. News* at 8984. (emphasis added).

reconciled with the manifest intent of Congress to eliminate artificial historic distinctions,[40] create "a single, national market," and put "an end to the economic distortions which accompanied the outdated mode of regulation under the Natural Gas Act."[41]

In view of the foregoing, it is clear that the Commission's jurisdiction to regulate pipeline production under the Natural Gas Act has been repealed. It has not been "repealed by implication," however, as petitioners suggest. It has been repealed by the express language of the NGPA, declaring that a new pricing regime has been established for all domestic gas production, not just the production of independent producers and affiliates.

II. The Court Below Properly Refused To Defer To An Agency Interpretation Which Was Manifestly Inconsistent With The Language, Legislative History, And Purposes Of The NGPA

Petitioners also claim that the court of appeals failed to accord sufficient deference to the Commission's interpretation of "first sale." Like their other claims, however, this contention is also without merit.

At the inception of its analysis, the court of appeals recognized that an agency's interpretation of a statute, while not controlling, is generally given deference. The court further recognized that comparatively more deference is granted when there is a longstanding interpretation which has not been disturbed by congressional action, *International Brotherhood of Teamsters* v. *Daniel*, 439 U.S. 551, 566 n. 20 (1979); the interpretation concerns a matter within the agency's expertise, *Adkins* v. *Hampton*, 586 F.2d 1070, 1073 (5th Cir. 1978); or the agency played a role in the development of the

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[40] S. Rep. No. 95-436, *supra*, at 21.

[41] *See* statement of Rep. Dingell, Chairman of House Committee on Interstate and Foreign Commerce, 124 *Cong. Rec.* 38361 (1978).

statute, *Ford Motor Credit Co.* v. *Milhollin*, 444 U.S. 555 (1980).

In this particular case, however, none of these factors was present. Since the term "first sale" had never been used by the Commission in its administration of the Natural Gas Act, the Commission obviously had not developed any unique expertise concerning the definition. For the same reason, there was no long-standing administrative interpretation which had been sanctioned by tacit congressional acceptance. Finally, the Commission readily conceded that it had no input whatsoever in the legislative development of the term "first sale." Under these circumstances, and because the Commission's regulation was interpretative in nature, rather than legislative,[42] the court reasoned that it could not blindly accept an interpretation of "first sale" which was manifestly inconsistent with "the clear meaning of a statute as revealed by its language, purpose and history." (App. A-7).

Notwithstanding petitioners' arguments to the contrary, the court of appeals' decision is totally consistent with well-established principles of statutory construction. Indeed, as this Court recently stated, "the courts are the final authorities on issues of statutory construction," and they "must reject administrative constructions of the statute . . . that are inconsistent with the statutory mandate or that frustrate the policy that Congress sought to implement." *Federal Election Commission* v. *Democratic Senatorial Campaign Committee*, 454 U.S. 27, 32 (1981); *see, also, Volkswagenwerk* v. *Federal Maritime Commission*, 390 U.S. 261, 272 (1968).

III. The Decision Below Does Not Encroach Upon State Jurisdiction Over Retail Sales Of Natural Gas

The Commission asserts that according "first sale" status to production by pipelines and distribution companies will "create

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[42] In *Batterton* v. *Francis*, 432 U.S. 416, 425 n. 9 (1977), a case cited by the lower court (App. A-6), this Court noted that *interpretative* regulations are accorded comparatively less deference than legislative regulations.

a substantial reworking of state and federal regulatory schemes in ways Congress could not have intended." (Comm. Br. 39). As the court of appeals recognized, however, there is no merit to this assertion.

The *only* change brought about by a non-discriminatory interpretation of "first sale" relates to the *wholesale price* of pipeline and distributor production. Consistent with Congressional intent to eliminate the artificial distinctions between the interstate market and the intrastate market, the price for this production, like the price of all production by independent producers and affiliates, will now be determined under the comprehensive structure of the NGPA.[43] All subsequent resales, however, will be regulated in precisely the same manner as they were prior to the NGPA.[44]

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[43] Contrary to Michigan's claim (Br. 10), the states are not precluded by the decision below from establishing rates for intrastate production which are lower than the NGPA ceiling prices. Section 602(a) states that nothing in the Act "shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price" under the NGPA. 15 U.S.C. (Supp. V) 3432(a).

[44] There is no merit to petitioners' sweeping allegation that the decision below would completely eradicate the Commission's jurisdiction under the Natural Gas Act to regulate the prices which interstate pipelines charge their resale customers. (Comm. Br. 13, AEPCO Br. 7-8). Indeed, Section 601 of the NGPA (entitled "Coordination With the Natural Gas; Miscellaneous Provisions"), 15 U.S.C. (Supp. V) 3431, harmonizes the provisions of the NGPA with the Commission's jurisdiction under the Natural Gas Act. Section 601(b)(1) provides that any amount paid in any first sale under the NGPA shall be deemed "just and reasonable" under Sections 4 and 5 of the Natural Gas Act, 15 U.S.C. 717c and 717d, if such amount does not exceed the maximum lawful prices set forth in Title I. Moreover, Section 601(c)(2)(B) requires the Commission to permit pipelines to flow-through any "just and reasonable" NGPA prices which are not excessive due to "fraud, abuse, or similar grounds." 15 U.S.C. (Supp. V) 3431(c)(2)(B). Finally, Section 601(a)(2) preserves, with minor

More specifically, all resales of pipeline production to distribution companies and other pipeline companies will be regulated by the Commission under the Natural Gas Act. Just as the Commission has historically determined the cost of certain pipeline production by reference to the area and nationwide rates—and, more recently, by reference to the NGPA rates (Order No. 98)—the costs of *all* such production will now be determined, as a matter of law, by reference to the NGPA. Likewise, the retail sales regulated by the states will now reflect the NGPA rates for pipeline or distributor production, in precisely the same manner as they reflect NGPA rates for production by independent producers and affiliates.

In short, the Commission's assertion of "jurisdictional problems" is transparent and indefensible. The Commission is perfectly capable of administering the NGPA in a manner which gives meaning to Congressional intent, without unduly impinging upon state prerogatives.

IV. Petitioners' Contentions Relating To "Windfall Profits" Are Inaccurate And Are Irrelevant To The Proper Construction Of The NGPA

Believing that any economic incentives above cost-based rates are unjustified, petitioners and *amici* speculate that treating pipeline producers on an equal basis with independent producers and affiliates will result in "windfall profits", particularly with respect to the so-called "old" pipeline production from pre-1973 wells on pre-October 8, 1969 leases. Specifically, it is alleged that consumers have already borne the risks for this so-called "old" production, and that, in any event, application of NGPA pricing structure to this production will not induce any additional exploration and development. (Comm. Br. 33-35).

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exceptions, the Commission's comprehensive jurisdiction under the Natural Gas Act over the transportation of natural gas in interstate commerce. 15 U.S.C. (Supp. V) 3431(a)(2).

These rhetorical arguments are largely irrelevant, because they focus upon the economic wisdom of the NGPA, rather than its meaning, as revealed by the language, history, and purposes of the Act.[45] Nonetheless, they must be briefly answered.

The initial flaw in petitioners' reasoning is the assumption that all of the so-called "old" production was developed with the expectation that it would be regulated on a cost-basis under the Natural Gas Act. As the Commission is undoubtedly aware, however, a significant amount of this production was developed by the pipelines prior to the enactment of the Natural Gas Act and long before the Commission announced that pipeline production must be priced on a cost-of-service basis.[46] At that time, pipelines certainly did not undertake to develop gas reserves on the assumption that any risks would be underwritten by the Commission's yet-to-be announced pricing policy.

In any event, it is untenable for petitioners to suggest that only independent producers and affiliates are entitled to the NGPA prices, because they alone bore the risks of unsuccessful ventures, while, in the case of pipeline production, these risks were borne by the consumer. As we have shown (*supra*, pp. 39-40), the area and nationwide rates permitted independent producers to charge the consumer for the costs of unsuccessful ventures. Moreover, the risks historically incurred by affiliated producers were identical to those borne by pipeline producers. *City of Chicago* v. *F.P.C.*, 458 F.2d 731, 737, n. 20 (D.C.Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972) (affiliate production "is treated for ratemaking purposes as if it were produced by the pipeline company itself."). It is thus clear that the alleged distinctions upon which petitioners construct their "windfall profits" argument are largely illusory.

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[45] It is well settled that "courts do not substitute their social and economic beliefs for the judgment of legislative bodies, who are elected to enact laws." *Ferguson* v. *Strupa*, 372 U.S. 726, 730 (1963).

[46] *See, e.g., Canadian River Gas Co.*, 3 F.P.C. 32 (1942), *aff'd sub nom. Colorado Interstate Gas Co.* v. *F.P.C.*, 324 U.S. 581 (1945).

There is no merit to petitioners' bold assertion that applying the NGPA prices to pipeline production will not result in additional gas supplies, because "[t]he only factors involved in the pipeline's determination to invest additional capital . . . are the needs of its customers and the relative cost of acquiring sufficient supply elsewhere." (Comm. Br. 34). Pipelines, like independent producers and affiliates, are also concerned about their expected return on investments in exploration and development in comparison with other investment opportunities. If pipelines are permitted to have their production priced under the NGPA, rather than under the archaic cost-based structure of the Natural Gas Act, they will undoubtedly invest more money in drilling new wells, "reworking" old wells, and acquiring new leases. For the petitioners to suggest otherwise is disengenuous and inconsistent with the underlying economic philosphy of the NGPA.

Finally, it must be emphasized that, to the extent there are legitimate distinctions between "old" and "new" gas, those distinctions have already been considered by Congress and have been largely maintained in the NGPA. Thus, the "first sale" price allowed by Section 104 for gas committed or dedicated to interstate commerce prior to the effective date of the Act is the "just and reasonable" price which was in effect prior to enactment of the NGPA. 15 U.S.C. (Supp. V) 3314. If the decision below is upheld—as it should be—a significant amount of the so-called "old" production will fall within this category.

Some of the "old" production will be produced from "stripper" wells (i.e., wells which produce less than 60 Mcf per day) and, therefore, may qualify for comparatively higher prices under Section 108 of NGPA. 15 U.S.C. (Supp. V) 3318. Contrary to petitioners' claim, however, the Section 108 prices will not create "pure profit" for the pipelines without any corresponding benefit to the consumer. (Comm. Br. 34-35, n. 35). Instead, the NGPA prices will permit these marginal wells, which might otherwise be "shut-in" for economic reasons, to continue to be operated and maintained. Thus, the consumer is assured of this important source of supply, which, incidentally, is priced at a lower level than certain other categories under the NGPA.

To place the impact of the decision in perspective, the Department of Energy statistics cited by the Commission demonstrate that approximately 95% of the nation's total gas production in 1981 was produced by independent producers, whose entitlement to the NGPA rates is not in controversy.[47] The remaining 5% was produced by pipelines or their affiliates. By virtue of Order Nos. 58 and 98, however, a substantial portion of this 5% would have qualified for the NGPA rates *prior to the court of appeals decision*, because it is either (a) produced by affiliates, or (b) produced by pipelines from post-1972 wells or post-October 7, 1969 leases. Thus, in economic terms, the decision below impacts upon only the fraction of interstate pipeline production which the Commission persists in seeking to regulate on a cost-of-service basis—specifically, production from pre-1973 wells on leases acquired prior to October 8, 1969, and production previously granted a special exemption for the area and nationwide rates. While applications of the NGPA prices to this production may increase the rates of certain pipelines to some extent, the impact of such increases will be minor in comparison to the impact of the Act on the rates charged by independent producers and affiliates.[48]

In the final analysis, petitioners' assertion of "windfall profits" is nothing more than a replay of the position taken before Congress in the 1977-78 debates by the opponents of the NGPA. After balancing the relevant economic interests, however, Congress rejected the argument and decided that a new pricing structure was necessary to encourage conservation and provide incentives for the development and maintenance of

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[47] *Energy Data Report, Domestic Natural Gas Reserves And Production Dedicated To Interstate Pipeline Companies, 1981*, at 2 (U.S. Dept. of Energy, July 27, 1982). See Commission Br. at 3, n. 3.

[48] At least one pipeline has taken the position that application of the NGPA price ceilings to its company-owned production would result in a *decrease* of $27.4 million in its annual revenues. See Memorandum Brief of Intervenor Northwest Pipeline Corporation (p. 3), filed with the court below on February 17, 1981.

supplies.[49] Thus, the court below did not decide that higher prices are appropriate as a matter of policy, as petitioners imply. It simply decided that the NGPA pricing structure designed by Congress was intended to apply without discrimination to *all* natural gas producers, not just the independent and affiliated producers championed by the Commission.

CONCLUSION

For the foregoing reasons, the decision below should be affirmed in all respects.

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[49] As the court observed in *Pennzoil Co.* v. *F.E.R.C.*, 645 F.2d 360, 379, n.37 (5th Cir. 1981), *cert. denied*, No. 81-340 (January 11, 1982), "Congress carefully considered the economic impact of the NGPA in designing the Act."

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Supplemental Respondent's Brief

81-1889

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IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK, *et al.*, *Petitioners.*

v.

MID LOUISIANA GAS COMPANY, *et al.*, *Respondents.*

On Writ Of Certiorari To The United States Court Of Appeals
For The Fifth Circuit

Motion to Supplement Listing of
Affiliates Pursuant to Rule 28.1

EL PASO NATURAL GAS COMPANY ("El Paso") respectfully moves to supplement the listing of affiliates pursuant to Rule 28.1 contained in the "Brief of Respondents Mid Louisiana Gas Company, El Paso Natural Gas Company, Colorado Interstate Gas Company, Kentucky West Virginia Gas Company, and Kansas-Nebraska Natural Gas Company, Inc." filed in this Court on January 11, 1983.

Since the filing of the aforementioned brief of Respondents, The El Paso Company's subsidiary, Geo Nuclear Nobel El Paso has been dissolved. Further, R. H. Holdings Corporation, a wholly owned subsidiary of Burlington Northern Inc. has acquired 47% of the common stock of The El Paso Company. Attached hereto is a listing of subsidiaries and affiliates of Burlington Northern Inc.

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Dated: March 19, 1983

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BN FINANCIAL SERVICES INC.

BN TIMBERLANDS INC.

BURLINGTON NORTHERN AIRMOTIVE INC.

BURLINGTON NORTHERN INTERNATIONAL SERVICES INC.

Burlington Northern Trading Company Inc.

The Belt Railway Company of Chicago (7.69%)

BN Transport Inc. -- BNT Terminals, Inc.

Colt Intermodal Inc.

Burlington Northern Dock Corporation

Burlington Northern (Manitoba) Limited

Burlington Northern (Oregon-Washington) Inc.

Burlington Northern Railroad Properties Inc.

Camas Prairie Railroad Company (50%)

Chicago Union Station Company (25%)

Clarkland, Inc.

Clarkland Royalty, Inc.

Davenport, Rock Island and

North Western Railway Company (50%)

The Denver Union Terminal Railway Company (33.33%)

Galveston Terminal Railway Company (50%)

Houston Belt & Terminal Railway Company (12.5%)

Iowa Transfer Railway Company (25%)

BURLINGTON NORTHERN RAILROAD COMPANY

Kansas City Terminal Railway Company (16.6%)

Keokuk Union Depot Company (40%)

The Lake Superior Terminal and

Transfer Railway Company (66.67%)

Longview Switching Company (33.33%)

The Minnesota Transfer Railway Company (33.33%)

905 Olive Corporation

BURLINGTON NORTHERN RAILROAD COMPANY (Con't)

Paducah & Illinois Railroad Company (33.33%)

Portland Terminal Railroad Company (40%)

The Pueblo Union Depot and Railroad Company (25%)

The Saint Paul Union Depot Company (40.2%)

Terminal Railroad Association of St. Louis (12.5%)

Trailer Train Company (9.7%)

Western Fruit Express Company

The Wichita Union Terminal Railway Company (33.3%)

Winona Bridge Railway Company (66.67%)

GLACIER PARK COMPANY

Dreyer Bros, Inc.

Tennessee Glacier Park Company

Washington BN Railroad Properties Inc.

Washington BN Timberlands Inc.

GLACIER PARK LIQUIDATING COMPANY

Washington Glacier Park Company

MERIDIAN LAND & MINERAL COMPANY

Butte Pipe Line Company (10%)

Northern Rockies Pipe Line Co.

MILESTONE PETROLEUM INC.

Osago Milestone Petroleum Inc.

Portal Pipe Line Company (50%)

Saxony Corporation

NEW MEXICO AND ARIZONA LAND COMPANY (50%)

NZ Development Corporation

NZ Properties, Inc.

PLUM CREEK INC.

R-H HOLDINGS CORPORATION

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, PETITIONER, vs. MID-LOUISIANA GAS COMPANY, ET AL.	)	
ARIZONA ELECTRIC POWER COOPERATIVE, INC., PETITIONER, vs. MID-LOUISIANA GAS COMPANY, ET AL.	)	Nos. 81-1889 81-1958 81-2042
STATE OF MICHIGAN, PETITIONER vs. MID-LOUISIANA GAS COMPANY, ET AL.	)	82-19
FEDERAL ENERGY REGULATORY COMMISSION, PETITIONER vs. MID-LOUISIANA GAS COMPANY, ET AL.	)	

CERTIFICATE OF SERVICE

I hereby certify that I have caused a copy of the attached Motion to Supplement Listing of Affiliates Pursuant to Rule 28.1 to be served on the parties hereto by delivering a copy by hand to the Office of the Solicitor General, Department of Justice, Washington, D.C. 20530 and by mailing by first class mail, postage prepaid, on all other parties listed on the attached service list this 19th day of March, 1983.

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Respondent's Brief

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*
Petitioners,

v.

MID LOUISIANA GAS COMPANY, *et al.*
Respondents.

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QUESTION PRESENTED

Whether Congress intended the incentive pricing provisions of the Natural Gas Policy Act of 1978 to apply to all domestic natural gas production, including all natural gas produced by interstate pipelines.

TABLE OF CONTENTS

	Page
STATEMENT OF THE CASE	1
A. The Natural Gas Policy Act	2
B. The FERC's Orders	4
C. The Opinion Below	5
SUMMARY OF ARGUMENT	5
ARGUMENT	7
I. THE STATUTORY LANGUAGE REQUIRES THE DECISION BELOW	7
A. The Decision Below Is Mandated By The Plain Language Of The Statute	7
B. Other Provisions Of The NGPA Support The Decision Below	10
II. THE DECISION BELOW IS CONSISTENT WITH THE LEGISLATIVE HISTORY OF THE NGPA	14
III. THE DECISION BELOW CORRECTLY REFLECTS THE ECONOMIC AND REGULATORY REALITIES OF THE "SALE" OF GAS PRODUCED BY PIPELINES	16
IV. THE PETITIONERS' INTERPRETATION WOULD LEAD TO INCONSISTENT AND ILLOGICAL RESULTS	20
V. THE DECISION BELOW DOES NOT RESULT IN A "WINDFALL"	22
CONCLUSION	29

TABLE OF AUTHORITIES

CASES — Page

American Commercial Lines, Inc. v. Louisville & Nashville Railroad Co., 392 U.S. 571 (1968) 23
American Tobacco Co. v. Patterson, 102 S. Ct. 1534 (1982) 7
Canadian River Gas Co. v. *Public Service Commission*, 3 F.P.C. 32 (1942), *aff'd sub nom. Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581 (1945) 26
Colorado Interstate Gas Co. v. FPC, 324 U.S. 581 (1945) 2, 26
Columbia Gas Development Corp. v. FERC, 651 F.2d 1146 (5th Cir. 1981) 14
Dawson Chemical Co. v. Rohm & Haas Co., 448 U.S. 176 (1980) 7
Ecee, Inc. v. FERC, 645 F.2d 339 (5th Cir. 1981) 20
Exxon Corp. v. Governor of Maryland, 437 U.S. 117 (1978) 23
Ferguson v. Skrupa, 372 U.S. 726 (1963) 23
FPC v. Louisiana Power & Light Co., 406 U.S. 621 (1972) 25
Great Plains Gasification Associates, 19 F.P.S. 5-540 (Nov. 21, 1979) 28
Gayler v. Wilder, 51 U.S. (10 How.) 477 (1850) 10
Hope Natural Gas Co., 3 F.P.C. 150 (1942), *aff'd sub nom. Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944) 26
International Brotherhood of Teamsters v. Daniel, 439 U.S. 551 (1979) 7
Olsen v. Nebraska ex rel. Western Reference & Bond Association, 313 U.S. 236 (1941) 23
Opinion No. 468, Area Rate Proceeding (Permian Basin Area), 34 F.P.C. 159 (1965), *aff'd sub nom. Permian Basin Area Rate Cases*, 390 U.S. 747 (1968) 24, 27
Opinion No. 568, Pipeline Production Area Rate Proceeding, 42 F.P.C. 738 (1969), *aff'd sub nom. City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972) 18

TABLE OF AUTHORITIES—Continued

	Page
Opinion No. 699-H, Just and Reasonable National Rates for Sales of Natural Gas, 52 F.P.C. 1604 (1974), *aff'd sub nom. Shell Oil Co. v. FPC*, 520 F.2d 1061 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976)	18
Opinion No. 770, National Rates for Jurisdictional Sales of Natural Gas, 56 F.P.C. 509 (1976), *aff'd sub nom. American Public Gas Association v. FPC*, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied sub nom. American Public Gas Association v. FERC*, 435 U.S. 907 (1978)	18
Opinion No. 749, 54 F.P.C. 3090 (1975)	26
Order No. 440, 46 F.P.C. 1148 (1971)	25
Panhandle Eastern Pipe Line Co. v. FPC, 324 U.S. 635 (1945)	26
Pennhurst State School & Hospital v. Halderman, 451 U.S. 1 (1981), *on remand*, 673 F.2d 647 (3d Cir.), *cert. granted*, 102 S. Ct. 2956 (1982)	10
Pennzoil Co. v. FERC, 645 F.2d 360 (5th Cir. 1981), *cert. denied*, 454 U.S. 1142 (1982)	23
Piedmont & Northern Railway Co. v. ICC, 286 U.S. 299 (1932)	8
Southern Natural Gas Co., Opinion No. 379, 29 F.P.C. 323 (1963)	25
Trans Alaska Pipeline Rate Cases, 436 U.S. 631 (1978)	21
United Carbon Co., 25 F.P.C. 181 (1961)	25
United States v. American Trucking Associations, 310 U.S. 534 (1940)	10, 21
United States v. An Article of Drug, 394 U.S. 785 (1969)	8
Watt v. Alaska, 451 U.S. 259 (1981)	16

STATUTES

Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3312-3394 (Supp. IV 1980)	
§ 2(21), 15 U.S.C. § 3301(21) (Supp. IV 1980)	7, 8
§ 2(21)(A)(v), 15 U.S.C. § 3301(21)(a)(v) (Supp. IV 1980)	9, 21

TABLE OF AUTHORITIES—Continued

	Page
§ 2(21)(B), 15 U.S.C. § 3301(21)(B) (Supp. IV 1980)	8
§ 101(b)(9), 15 U.S.C. § 3311(b)(9) (Supp. IV 1980)	26
§§ 102-109 of Title I, 15 U.S.C. §§ 3312-3319 (Supp. IV 1980)	3, 10
§ 107(c)(1), (2), (3), (4), 15 U.S.C. § 3431 (Supp. IV 1980)	3
§ 108, 15 U.S.C. § 3318 (Supp. IV 1980)	23
§ 203(b)(2), 15 U.S.C. § 3343(b)(2) (Supp. IV 1980)	11
§ 311, 15 U.S.C. § 3371 (Supp. IV 1980)	3
§§ 401-404, 15 U.S.C. §§ 3391-3394 (Supp. IV 1980)	3
§ 601, 15 U.S.C. § 3431 (Supp. IV 1980)	3
§ 601(b)(1)(E), 15 U.S.C. § 3431(b)(1)(E) (Supp. IV 1980)	12, 13
National Gas Act, §§ 717-717w (1976)	
15 U.S.C. § 717c(e) (1976)	25

REGULATIONS

18 C.F.R. pt. 201, Account Nos. 304-87 (1981)	19
18 C.F.R. pt. 201, Instruction 12B (1981)	19
18 C.F.R. § 154.38(d)(4) n.1 (1981)	18

MISCELLANEOUS

123 Cong. Rec. S15550-51, S15559, S15562 (daily ed. Sept. 24, 1977)	23
123 Cong. Rec. S15551, S15553, S15563 (daily ed. Sept. 24, 1977)	23
123 Cong. Rec. S15608 (daily ed. Sept. 26, 1977)	23
124 Cong. Rec. H13114 (daily ed. Oct. 14, 1978)	14
124 Cong. Rec. H13118 (daily ed. Oct. 14, 1978)	11
Energy Data Reports, Domestic Natural Gas Reserves And Production Dedicated To Interstate Pipeline Companies, 1981, at 2 (Dept. of Energy, July 27, 1982)	22

TABLE OF AUTHORITIES—Continued

Page

Hearings on H.R. 6831 Before the Subcommittee on Energy and Power of the House Committee on Interstate and Foreign Commerce, 95th Cong., 1st Sess. 894 (1977) (testimony of David D. Schwartz) 15

H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 116, *reprinted in* 1978 U.S. Code Cong. & Ad. News 8800 17

S. 2104, 95th Cong., 1st Sess. (1977) 13

S. Rep. No. 95-436, 95th Cong., 1st Sess. (1977) 15

Petroleum Intelligence Weekly (October 18, 1982) 28

Stripper Well Natural Gas; Final Regulations and Amendments to Interim Regulations, 44 Fed. Reg. 49,656 (Aug. 24, 1979) 23

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

Nos. 81-1889, 81-1958, 81-2042 and 82-19

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*,
Petitioners,

v.

MID LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF FOR RESPONDENT CONSOLIDATED GAS SUPPLY CORPORATION

Consolidated Gas Supply Corporation ("Consolidated"), a petitioner below and a Respondent here, files this brief in response to the briefs filed by Petitioners Federal Energy Regulatory Commission ("FERC" or "Commission"), Public Service Commission of the State of New York ("New York"), Arizona Electric Power Cooperative, Inc. ("AEPCO"), and the State of Michigan ("Michigan") (hereinafter collectively referred to as "Petitioners"), and various parties supporting the Petitioners as amici curiae. Consolidated urges this Court to affirm the decision below.

STATEMENT OF THE CASE

This case concerns whether Congress intended natural gas produced by an interstate pipeline company and sold as a part of its system supply to qualify for "first sale" treatment under the Natural Gas Policy Act of 1978 ("NGPA" or "Act"). In Order No. 58, the FERC decided that natural gas produced by an interstate pipeline

company could qualify for "first sale" treatment only if sold in the field, or if sold under a contract committing the production from an identifiable well to a particular pipeline customer. By excluding all other sales of pipeline production from qualifying as "first sales"—by far the bulk of pipeline production—the FERC asserts authority under the Natural Gas Act ("NGA") over the price of virtually all interstate pipeline production.[1]

The court below vacated the FERC's order, finding that the language, purpose, and history of the NGPA left the FERC no authority under the NGA to control the price of any domestically-produced natural gas. The court held that the initial sale of all domestic production qualifies for "first sale" treatment.

A. The Natural Gas Policy Act

Congress enacted the NGPA specifically to end the severe shortage of natural gas that confronted interstate pipelines and their customers in the late 1970's by encouraging maximum domestic production through incentive pricing. Thus, the NGPA establishes a comprehensive and uniform statutory pricing structure for all "first sales" of natural gas sold in the interstate and intrastate markets.[2]

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[1] A glossary of terms used in the application of the NGPA to the natural gas industry is attached hereto as Appendix A. Additionally, "App.", as used in this Brief, refers to the appendix to the petition for a writ of certiorari filed in No. 81-1889.

[2] Although interesting for its historical value, the discussion of the Sisyphean labors of the Federal Power Commission to impose cost-based regulation on domestic natural gas production, set forth in Petitioners' briefs and chronicled in several decisions of this Court, is of little if any pertinence to this case. It was this forty years of regulatory failure that finally compelled the Congress to control legislatively the pricing of natural gas production. The NGPA is the very expression of congressional intent to effectuate "fair field pricing" of pipeline production for which this Court searched in vain in *Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581, 601 (1945).

Congress divided the NGPA into six titles. Title I establishes the various maximum lawful prices for all domestic natural gas production.[3] Title II requires that natural gas produced or purchased by pipelines and sold to industrial users be incrementally priced to shield residential gas users from the impact of some of the price increases resulting from Title I.[4] Title III facilitates the interstate movement of natural gas by immunizing from regulation under the NGA certain transportation and sale arrangements between intrastate and interstate natural gas companies.[5] Title IV establishes a national gas curtailment policy to be applied in times of shortage,[6] and Title V grants to the FERC general enforcement and rulemaking powers to effectuate the purposes of the Act. Title VI coordinates the NGPA with the NGA and identifies areas where NGA cost-based regulation is no longer applicable.[7]

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[3] The prices vary according to the particular classification of production and apply to all "first sales." The various classifications are set forth in sections 102-109 of Title I of the NGPA. 15 U.S.C. §§ 3312-3319 (Supp. IV 1980). The pricing provisions of Title I do not restrict the maximum prices to gas produced by independent producing companies. No distinctions are made based on the identity of the producer. The pricing provisions simply fix a "maximum lawful price" for each category of gas. *See infra* notes 14-23 and accompanying text.

[4] 15 U.S.C. §§ 3341-3348 (Supp. IV 1980).

[5] *See, e.g.*, NGPA § 311, 15 U.S.C. § 3371 (Supp. IV 1980). Thus, contrary to the assertion of the FERC (FERC Brief, at 29), Congress expressly sought to alter pipeline distribution routes to provide all producers equal access to the interstate market.

[6] NGPA §§ 401-404, 15 U.S.C. §§ 3391-3394 (Supp. IV 1980).

[7] NGPA § 601, 15 U.S.C. § 3431 (Supp. IV 1980). Title VI excludes from the FERC's NGA jurisdiction all gas that was not committed or dedicated to interstate commerce as of November 8, 1978, and also removes from Commission jurisdiction all committed and dedicated gas qualifying under NGPA sections 107(c)(1)-(4), 102(c), and 103(c). With respect to the transportation of natural gas, Title VI eliminates Commission NGA jurisdiction over certain transactions authorized in Title III of the Act.

B. The FERC's Orders

To implement the NGPA, the FERC promulgated final regulations that determined which sales by interstate pipelines would qualify as "first sales." Distinguishing between production by pipelines and distribution companies, and production by any other producer, including affiliates of pipelines and affiliates of distributors, the FERC refused to recognize that production sales by pipelines and distribution companies were "first sales" unless (1) the production is sold in an off-system sale at the wellhead, or (2) the production is committed by contract to a particular customer from an identifiable source. (App. B-2, B-3.) The FERC conceded that, as a result of its definition, "most sales by interstate pipelines will not qualify as first sales . . . ." (App. B-3.)[8]

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[8] The Commission subsequently issued Order No. 98 which promulgated regulations under the NGA governing the wellhead price of interstate pipeline production sold in mixed volume sales. (App. B-14 to B-49.) The regulations permitted, as a matter of Commission *discretion*, pipeline production previously priced on an area-wide or nationwide cost basis to be priced at the level that would have been applicable under Title I of the NGPA were such sales "first sales," provided the applicable NGPA rates did not exceed the amount paid in "comparable sales" by nonaffiliated producers. (App. B-47.) The Commission thereby recognized the intracorporate transfer of production volumes as a "sale," despite the fact that the production volumes are subsequently mixed with purchased gas and become a part of the pipeline's system supply. The Commission found this NGPA parity pricing necessary to encourage that production, and administratively feasible, although it maintained in Order No. 58 that "the source of the particular volumes of gas sold generally cannot be determined" where pipeline produced gas is mixed with purchased gas. (App. B-5.) In Order No. 98, the FERC also held, however, that pipeline production previously priced on a cost of service basis would not be subject to the NGPA pricing provisions, but would continue to be subject to FERC cost of service regulation under the NGA. (App. B-27.)

C. The Opinion Below

The court below held that Congress "clearly intended" any natural gas produced by an interstate pipeline, intrastate pipeline, local distribution company, or any affiliate thereof, to be accorded "first sale" status under the NGPA regardless of the contractual form of the transaction or the corporate form of the producer. (App. A-15.) This holding was predicated on a thorough analysis of the statute, including its language, purpose, and legislative history. The court reasoned that the FERC's order excluding pipeline production from the NGPA pricing structure was inconsistent with the overriding purpose of the Act—to enhance the supply of gas in the interstate market by providing pricing incentives that would encourage maximum natural gas exploration and development. (App. A-9.)

SUMMARY OF ARGUMENT

Petitioners and amici recognize that the paramount purpose of the NGPA was to eliminate the natural gas shortages faced by interstate pipelines and their customers by encouraging the exploration, development, and recovery of gas through a uniform, incentive-pricing scheme applicable to both the interstate and intrastate markets. In its "Question Presented," the FERC concedes that the congressionally-established pricing scheme was intended to reach gas produced by pipelines as well as independent producers. Nonetheless, the FERC contends that Congress did not intend the NGPA incentive prices to apply to most of the gas produced by interstate pipeline, *i.e.*, to the same interstate market that was unable to acquire adequate gas supplies under the NGA.

Petitioners are unable to point to any language or legislative history to support the exclusion of most pipeline production from the ambit of the NGPA. They argue,

however, that there is no "sale" of pipeline-produced gas at the location where gas is transferred from the production division to the transmission division of the pipeline. Petitioners suggest that if there is no "sale" at the wellhead, there can never be a "first sale."

Petitioners' contention ignores the reality that gas produced by a pipeline—whether or not mixed with gas purchased from others—*is sold at some point* for resale or consumption. The court below concluded that Congress intended to recognize this sale at the point of the intracorporate transfer in the producing field, thereby placing pipeline production on parity with gas purchased from others. This is precisely what the FERC itself had done in pricing pipeline-produced gas at area-wide, nationwide, or NGPA levels. Regardless of where the sale takes place, it is undeniable that at some point, there is a "sale" of pipeline-produced volumes. That sale is a "first sale."

To elicit a sympathetic response, Petitioners suggest that "windfall" profits will result from the decision below. This suggestion is totally without merit. The "windfall" allegations merely echo the arguments unsuccessfully made by Petitioners before Congress. These arguments, having been fully considered and rejected by Congress, should not be reconsidered here.

ARGUMENT

I. THE STATUTORY LANGUAGE REQUIRES THE DECISION BELOW

Adhering to the basic tenet of statutory construction that the starting point is the language of the statute itself, *see, e.g., American Tobacco Co. v. Patterson*, 102 S.Ct. 1534, 1537 (1982); *Dawson Chemical Co. v. Rohm & Haas Co.*, 448 U.S. 176, 187 (1980); *International Brotherhood of Teamsters v. Daniel*, 439 U.S. 551, 558 (1979), the court below unanimously held that the "first sale" definition unambiguously includes any and all natural gas produced by any producer, including interstate pipelines.

A. The Decision Below Is Mandated By The Plain Meaning Of The Statute

NGPA section 2(21) is expresesd in terms of a General Rule[9] and an exception to the General Rule. The General Rule begins with the statement that the term "first sale" means

> any sale of any volume of natural gas—
>
> (i) to any interstate pipeline or intrastate pipeline;
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> (ii) to any local distribution company;
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> (iii) to any person for use by such person;
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> (iv) which precedes any sale described in clauses (i), (ii), or (iii); and
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> (v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this Act.[10]

This includes *every* sale of *any* volume of natural gas sold to a pipeline, to a local distribution company, or to an

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[9] NGPA § 2(21), 15 U.S.C. § 3301(21) (Supp. IV 1980).

[10] *Id.* § 3301(21)(A).

end user. Because sales of natural gas by interstate pipeline companies, whether of their own production or of production purchased from others, are generally sold to other pipelines, to local distribution companies, or to end users, all sales by pipelines would be "first sales" under the General Rule. Obviously, had the definition ended here, pipelines and distributors that resold natural gas purchased from others would be prevented from earning any return *of* or *on* transmission and distribution investments made downstream of production facilities. To avoid this result, the statute excludes from the General Rule

> the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof . . . .[11]

Without any qualifying language, the exclusion would preclude a pipeline company from ever engaging in a "first sale" of its own production. But Congress added a second, inclusory clause restricting the exclusion from the General Rule:

> unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

This inclusory clause limits the exclusion to natural gas that is not produced by a pipeline, local distribution company, or an affiliate of a pipeline or a local distdibution company. Natural gas produced and sold by those entities is, therefore, still subject to the General Rule.[12]

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[11] *Id.* § 3301(21)(B).

[12] It is well settled that exclusions from the general application of remedial statutes, such as the NGPA, are to be narrowly construed, and inclusory language, such as the "unless clause," is to be broadly construed to effectuate the purposes of the Act. *See, e.g.*, United States v. An Article of Drug, 394 U.S. 785, 799 (1969); Piedmont & N. Ry. Co. v. ICC, 286 U.S. 299, 311-12 (1932).

The court below properly concluded that the FERC's interpretation "would effectively read the second part of this subsection out of the NGPA. By over-stressing the first provision that sales by a pipeline are not first sales, the Commission would render the unless clause of subsection (B) a nullity." (App. A-8.)

The court's analysis is unconfutable. As the all-embracing language of the General Rule indicates, Congress envisioned that all domestic natural gas production would be subject to the statutorily-prescribed ceiling prices until it is resold.

The all-inclusive nature of the General Rule is further evident from section 2(21)(A)(v) which empowers the FERC to *include* any sales not otherwise defined as "first sales" within the definition of the term "first sale," if necessary to avoid circumvention of Title I. Significantly, Congress did not empower the FERC to exclude sales which are otherwise included in the definition. The universe of "first sales" can only be expanded, not contracted.

The decision below gives meaning to each subpart of section 2(21). The "unless clause" is necessary to preserve the symmetry of the statute, which subjects all domestic production to the ceiling price limitations set by Congress, but preserves FERC price regulation over resales of such production. Without the "unless clause," natural gas produced by pipelines would be unrestricted by the statutory ceiling prices. As the Court of Appeals stated:

> Nothing in the language used here or elsewhere in the NGPA suggests any intent to deny NGPA pricing to natural gas just because it is produced by a pipeline. To the contrary, the unless clause of subsection (B) can only have meaning if it is interpreted as granting "first sale" status to gas which is attributable to pipeline production.[13]

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[13] App. A-8 to A-9.

B. Other Provisions Of The NGPA Support The Decision Below

The NGPA is divided into six titles. The term "first sale" is used in five of the six titles. The definition of that term applies equally to each title. It must necessarily carry the same meaning.[14]

Title I uses the term "first sale" in each section that establishes a maximum lawful price for a particular category of production. The opening subsection (a) of each section contains the phrase: "[t]he maximum lawful price . . . shall apply to any first sale of natural gas delivered during any month in the case of——." [15] Each section then delineates the criteria for price qualification. The criteria relate only to the nature of the gas and the nature of the well from which it is produced. The wells addressed in the sections include those already drilled, the gas from which is already committed or dedicated to interstate commerce, and those to be drilled, the gas from which is not yet committed or dedicated to interstate commerce. None of the sections distinguish among production based upon either the corporate form of the producer or the contractual form of the transaction.

Nor did Congress indicate that the eligibility for statutory prices would depend in any way upon the corporate form of the producer or the contractual form of the transaction. Quite the contrary. Congressman John D. Dingell, NGPA House Floor Manager, stated: "[s]ection 104 is not limited to existing contracts and succes-

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[14] As this Court historically has recognized, statutes must be read and construed as a whole. Pennhurst State School & Hospital v. Halderman, 451 U.S. 1, 18-19 (1981); United States v. American Trucking Ass'ns, 310 U.S. 534, 542-43 (1940); Gayler v. Wilder, 51 U.S. (10 How.) 477, 496 (1850).

[15] NGPA §§ 102-109, 15 U.S.C. §§ 3312-3319 (Supp. IV 1980).

sors to existing contracts but is applicable to *any* interstate gas for which a just and reasonable rate exists." [16] The use of the term "any" cannot be reconciled with Petitioners' suggestion that some pipeline production is to be treated differently from all other production.

The congressionally-recognized need for economic incentives to ensure full recovery of reserves from existing wells, and to drill for and produce new high-cost gas, is not limited to large producers. Nor is it limited to small producers not affiliated with pipelines or producers. Rather, it applies equally to all producers.[17]

Title II of the NGPA provides an incremental pricing mechanism for passing through, primarily to industrial end users, certain of the increased prices for "first sales" of natural gas. With respect to interstate pipelines, Congress provided that only certain portions of their acquisition costs of natural gas would be subject to the incremental pricing provisions. Section 203(b)(2) provides that for "any natural gas *produced by any interstate pipeline* or any affiliate of such pipeline, the first sale acquisition cost of *such* natural gas shall be determined in accordance with rules prescribed by the Commission." [18]

Reading this subsection in the context of the "first sale" definition, the court reasoned:

> By referring to the "first sale acquisition cost of *such* gas," in terms of "any gas produced by any interstate pipeline," Congress must have contemplated that any gas produced by a pipeline would be subject to a first sale. Moreover, the fact that Congress provided that the "first sale acquisition cost" of pipeline produced gas would, like the first sale price paid to inde-

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[16] 124 Cong. Rec. H13118 (daily ed. Oct. 14, 1978) (emphasis added).

[17] *See infra* note 43.

[18] 15 U.S.C. § 3343(b)(2) (Supp. IV 1980) (emphasis added).

> pendent producers, be passed along to the pipeline's ultimate customers suggests that both prices were to be treated in a similar manner.

(App. A-11 to A-12.) Congress clearly contemplated that natural gas produced by a pipeline would be the subject of a "first sale" when it referred to the "first sale acquisition cost" of pipeline-produced gas. Congress must have assumed that there would be a Title I "first sale" price for all pipeline-produced gas which would be incrementally priced under Title II.

Title VI generally coordinates the NGPA with the NGA. One of its provisions, the "Affiliated Entities Limitation" of section 601(b)(1)(E) provides that:

> For purposes of paragraph (1), in the case of any first sale *between* any interstate pipeline and any affiliate of such pipeline, any amount paid in any first sale shall be deemed to be just and reasonable if, in addition to satisfying the requirements of such paragraph, such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.[19]

Petitioners contend that section 601(b)(1)(E) applies only to sales of production by producers to their pipeline affiliates and does not apply to sales of production by pipelines to their distribution affiliates. (FERC Brief, at 23-24 & n.27; AEPCO Brief, at 9-10; New York Brief, at 17, 20-21.) Such a contention ignores the plain meaning of the word "between" used in section 601(b)(1)(E). Section 601(b)(1)(E), on its face, applies not only to "first sales" *by* affiliated producers *to* their pipelines, but also to sales of production *by* pipelines *to* their affiliates.[20]

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[19] *Id.* § 3431(b)(1)(E) (emphasis added).

[20] Elsewhere, Petitioners contend that the word "attributable" means "comprised exclusively." (FERC Brief, at 16-18; New York Brief, at 12-24.) Coupled with Petitioners' contention that the word "between" means "to," one can only assume that the Petitioners used George Orwell's *1984* as their lexicon.

The legislative history of section 601(b)(1)(E) establishes that the section specifically applies to "first sales" of pipeline-produced gas. The Senate precursor to the NGPA contained language that would have expressly applied a comparable transactions standard to sales of pipeline-produced gas by amending sections 4(e) and 5(a) of the NGA.[21] The Senate language was deleted in conference, but the Conference Committee achieved the same result by adding section 601(b)(1)(E). The working papers of the Conference Committee confirm that section 601(b)(1)(E) was intended to accomplish the same result as the Senate Bill,[22] and indicate beyond any doubt that the phrase "sales between affiliated entities" in the NGPA was intended to be equivalent to the language of the earlier Senate Bill that expressly included pipeline-produced volumes.

Thus, the term "first sale" as used in the various titles of the NGPA demonstrates conclusively that Congress intended to accord "first sale" status to *all* pipeline production.

The FERC concedes as much. In its statement of the "Question Presented," the FERC states that "[u]nquestionably, this scheme was meant to reach gas produced and sold at the wellhead by independent producers and pipeline producers." Without taking issue at this point with the meaning of the words "at the wellhead," [23] it is clear that the FERC acknowledges that Congress did not intend to exclude from the "first sale" definition natural gas produced by interstate pipelines. What the FERC has left for this Court to determine is whether Congress intended to treat a portion of pipeline-produced gas differently from the rest of pipeline-produced gas solely because some of the production is mixed with gas

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[21] S. 2104, 95th Cong., 1st Sess. (1977).

[22] *See* Appendix B.

[23] *See infra* p. 19.

purchased from other sources and is sold as a part of the pipeline's system supply.

II. THE DECISION BELOW IS CONSISTENT WITH THE LEGISLATIVE HISTORY OF THE NGPA

The FERC recognizes that the NGPA represents a "[c]ongressional decision to reorder the economic regulation of natural gas prices to provide a uniform system of statutorily prescribed price incentives."[24] As the Commission explained:

> Congress established a unified pricing scheme imposing maximum lawful prices for first sales by producers of domestically produced natural gas. The elimination of the dual market and the statutorily embraced commitment to price incentives are the cornerstones of the Congressional plan to encourage maximum production of natural gas.[25]

This concept of creating a "unified pricing scheme" is reflected in the comment of Congressman John D. Dingell, made late in the legislative process:

> The most important provisions of the bill are those which deal with wellhead pricing. These establish a schedule of price ceilings applicable to specifically defined categories of gas production. The result is creation of a single, national market for natural gas and an end to the economic distortions which accompanied the outdated mode of regulation under the Natural Gas Act.[26]

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[24] App. B-25. Yet, inconsistently, the FERC cites *Columbia Gas Development Corp. v. FERC* for the proposition that the NGPA was not intended to alter regulatory practice. (FERC Brief, at 26, 31, 35, 36.) A careful reading of that case, however, reveals that it stands only for the much narrower proposition that the NGPA does not supersede prior FERC certificate conditions that required producers to waive their contractual authorization to collect higher future prices in exchange for the present right to collect above-ceiling rates.

[25] App. B-23 to B-24.

[26] 124 Cong. Rec. H13114 (daily ed. Oct. 14, 1978).

It is obvious that this "unified pricing scheme" supplants traditional cost of service pricing. The report of the Senate Committee on Energy and Natural Resources explains:

> Natural gas price regulation based on historic costs was workable when there were abundant supplies of natural gas . . . . Producer claims that historic cost-based regulation is no longer appropriate for a premium fuel in short supply are fundamentally correct . . . . The shift in the natural gas market from surpluses to shortages requires the abandonment of historic cost-based regulation and of the artificial distinction between interstate and intrastate markets.[27]

Moreover, as noted in testimony before the House Subcommittee on Energy and Power:

> There is no doubt that the major interstate pipelines . . . will benefit from the pricing provisions because all of them have producing affiliates or divisions.[28]

The purposes of the NGPA are not served by creating a distinction between pipelines and independent producers, or among pipeline producers. As the court below properly held, Petitioners' interpretation would defeat the legislative goals of the NGPA:

> In achieving the goal of increasing natural gas production, pipeline producers deserve the price encouragement of NGPA no less than other producers.
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> * * * *
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> With respect to the goal of eliminating a dual market structure, the Commission's order would ex-

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[27] S. Rep. No. 95-436, 95th Cong., 1st Sess. 20-21 (1977).

[28] Hearings on H.R. 6831 Before the Subcommittee on Energy and Power of the House Committee on Interstate and Foreign Commerce, 95th Cong., 1st Sess. 894 (1977) (testimony of David D. Schwartz).

> clude virtually all interstate pipeline, intrastate pipeline and local distribution company production from the NGPA's uniform prices. While the Commission would retain control of interstate pipeline production under the NGA, the effect of its order would be to leave intact state regulation of intrastate pipeline and local distribution company production. The intrastate market for such production would thus be perpetuated. This would leave a substantial vestige of the dual market structure Congress sought to eliminate.

(App. A-9 to A-10.)

The FERC concedes that there is "relative silence" in the legislative history to support its interpretation (FERC Brief, at 25), and acknowledges that "[t]he silence of Congress may provide a treacherous guide to its intent." *Watt v. Alaska*, 451 U.S. 259, 271 n.13 (1981). The FERC also concedes that the NGPA was meant to reach gas produced by independent and pipeline producers. (FERC Brief, at (I).) Nonetheless, despite the clear expressions of congressional intent, the FERC would create an exception to the NGPA's uniform pricing scheme and would conclude that pipeline production mixed with other production is never the subject of a sale. Such a result belies economic and regulatory realities.

III. THE DECISION BELOW CORRECTLY REFLECTS THE ECONOMIC AND REGULATORY REALITIES OF THE "SALE" OF GAS PRODUCED BY PIPELINES

Unable to point to any language or legislative history to support their contention that Congress meant to continue regulation of pipeline production under the NGA, Petitioners rely entirely upon the attenuated argument that the transfer from the pipeline's production division to its transmission division does not meet the traditional criteria of a "sale" and, therefore, does not constitute a "sale" within the conventional definition of the term,

or a "first sale" under the NGPA. (*See* FERC Brief, at 19; New York Brief, at 25-27; AEPCO Brief, at 31; Michigan Brief, at 12-13.) Such a contention reflects a strained, academic approach to statutory construction, and defies natural gas industry realities and pre-existing regulatory practice.

Natural gas that is produced by a pipeline and mixed with natural gas purchased from others before being sold downstream is clearly sold under any definition of the term "sale." Exactly *where* the "sale" takes place is irrelevant to a determination of *whether* there is a "first sale" under the NGPA. To impute the "first sale" to a transaction at the wellhead, as the court below concluded that Congress contemplated, is consistent with the NGPA, industry practice, and pre-existing FERC regulation.

The Conference Report supports the court's conclusion. In discussing the FERC's power to define terms in the NGPA, the Conferees stated:

> [T]he Commission may define terms such as "transfer for value" used in the definition of first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition.[29]

This assumes that intracorporate transfers fall within the "first sale" definition. Congress merely committed to the Commission's judgment whether regulations were necessary to govern those transfers: "The fact that the Commission was permitted to regulate intracorporate transactions under the first sale definition does not imply that Congress did not intend in the first instance for them to be treated as first sales." (App. A-13.)

That the point of the intracorporate transfer is the point of the imputed "sale" is completely consistent with FERC and court precedent. Under the FERC's rules and

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[29] H.R. Rep. No. 95-1752, 95th Cong., 2d Sess. 116, *reprinted in* 1978 U.S. Code Cong. & Ad. News 8800, 9033.

policies promulgated before the enactment of the NGPA, the value of gas produced by pipelines for system supply was based upon the area-wide or nationwide rates applicable to sales by independent producers.[30] The FERC recognized that the only way to implement the parity pricing policy articulated in its opinions was to impute or attribute a sale to a transaction at or near the wellhead and to apply the applicable area-wide or nationwide rate at that point. This is precisely what the Commission has done in numerous pipeline rate proceedings since 1969.

The FERC's recognition of an imputed intracorporate sale of pipeline production is also illustrated by the purchased gas adjustment (PGA) clause prescribed by the Commission's regulations for inclusion in pipeline tariffs.[31] Under a PGA clause, a natural gas pipeline company may automatically flow through to its customers changes in the cost of its "purchased gas." The regulations define "purchased gas" to include the cost of pipeline production "that qualifies for and is being afforded an area of [sic] nationwide rate."[32]

The FERC recognizes the intracorporate "sale" of pipeline production. Where there is an imputed "purchase,"

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[30] In Opinion No. 568, Pipeline Production Area Rate Proceeding, Opinion No. 568, 42 F.P.C. 738 (1969), *aff'd sub nom.* City of Chicago v. FPC, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972), the Commission priced pipeline-produced gas at the area rate applicable to sales by independent producers. Similarly, in Opinion Nos. 699-H, Just and Reasonable National Rates for Sales of Natural Gas, Opinion No. 699-H, 52 F.P.C. 1604 (1974), *aff'd sub nom.* Shell Oil Co. v. FPC, 520 F.2d 1061 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976), and Opinion No. 770, National Rates for Jurisdictional Sales of Natural Gas, Opinion No. 770, 56 F.P.C. 509 (1976), *aff'd sub nom.* American Public Gas Ass'n v. FPC, 567 F.2d 1016 (D.C. Cir. 1977), *cert. denied sub nom.* American Public Gas Ass'n v. FERC, 435 U.S. 907 (1978), the Commission extended nationwide rate treatment to gas produced from wells commenced on or after January 1, 1973, by pipelines and their affiliates regardless of the lease acquisition date.

[31] 18 C.F.R. § 154.38(d)(4) n.1 (1981).

[32] *Id.*

it follows perforce that there is an imputed "sale."[33] Obviously, Petitioners' suggestion that an intracorporate sale is a fiction created by the court below[34] ignores what the FERC has done in prior orders and proposed to do in Order No. 98. (App. B-47.)[35]

In an attempt to buttress their position, Petitioners make the hollow argument that because the term "first sale" is used in Title I, entitled "Wellhead Pricing," downstream sales of pipeline production were not intended by Congress to be "first sales." (FERC Brief, at 22, 24; New York Brief, at 13 & n.12.) As discussed above,[36] the term "first sale" is used in five of the six Titles of the NGPA. It is not defined in Title I. The term "wellhead pricing" in Title I refers to where the *price* is to be applied, not where the sale takes place. FERC Order No. 58 concedes as much by recognizing that downstream sales exclusively attributable to pipeline production are "first sales," although not made at the wellhead and often made far from the wellhead. (App. B-3). The heading of Title I is not evidence of an intent to exclude pipeline-produced gas from the "first sale" definition.

Based upon the clear statutory language and supporting legislative history, the court below concluded that the FERC should recognize the intracorporate transfer from the producing division to the transmission division of the pipeline as a "sale." But whether the FERC is required to do so, or whether it may recognize that a sale of pipe-

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[33] In addition, the FERC regulations applicable to natural gas pipelines require the maintenance of operating or accounting records on a wellhead basis, 18 C.F.R. pt. 201, Instruction 12B (1981). Additionally, plant accounts are recorded on the basis of the pipeline's functions, such as production, storage, transmission, and distribution. *See* 18 C.F.R. pt. 201, Account Nos. 304-87 (1981).

[34] Michigan Brief, at 3-4. *See also* FERC Brief, at 15; New York Brief, at 10, 35; AEPCO Brief, at 12, 30, 33.

[35] *See supra* note 8.

[36] *See supra* notes 14-23 and accompanying text.

line-produced volumes actually occurs downstream, is immaterial. As the FERC itself has acknowledged:

> The prices prescribed in Sections 102 through 109 are not maximum lawful prices for "wellhead sales" but lawful prices for "first sales" . . . . A "first sale" is determined on the basis of who purchases the gas, *not* where the sale is made.[37]

Thus, the "first sale" could be recognized either at the well-head, as contemplated by Congress, or downstream where the pipeline-produced gas is sold to the pipelines' customers. The FERC's orders do neither and, accordingly, were properly vacated by the court below.

IV. THE PETITIONERS' INTERPRETATION WOULD LEAD TO INCONSISTENT AND ILLOGICAL RESULTS

Petitioners' suggestion that Congress sought to deny "first sale" status only to that portion of pipeline production that is mixed with gas purchased from others would lead to a crazy quilt of inconsistent and illogical regulatory results. Despite the express congressional desire to eliminate the bifurcated natural gas market that diverted gas out of the interstate market and contributed significantly to the gas shortages of the 1970's, Petitioners argue for the creation of a trifurcated market. Under Petitioners' approach: (1) certain interstate pipeline production would be priced under the NGA on the basis of historical cost of service for each pipeline; (2) all independent producer and affiliate production and all pipeline and local distribution company production sold in off-system sales would be subject to NGPA "first sale" maximum lawful prices; and (3) certain intrastate and local distribution company production would be priced at levels determined by state regulatory commissions. This hodgepodge of regulated prices was certainly not what Congress intended when it enacted a uniform pricing scheme

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[37] Brief for the Federal Energy Regulatory Commission at 22, Ecee, Inc. v. FERC, 645 F.2d 339 (5th Cir. 1981) (emphasis added).

to eliminate price disparities in the interstate and intrastate markets.[38]

There is no indication either in the NGPA or its legislative history that Congress intended to treat pipeline producers differently from independent producers or intended to distinguish among pipeline producers. Indeed, it has long been industry practice for pipeline producers to participate in drilling wells with independent producers or in joint ventures. Under the Petitioners' interpretation of the NGPA, pipeline producers would receive a price based on cost of service, although independent producers or co-venturers would receive NGPA prices for production from the same well or lease.[39]

Petitioners' position would also elevate corporate form over substance. Some interstate pipelines conduct their production activities through affiliates or wholly-owned subsidiaries, which Petitioners concede entitles them to NGPA prices. Other interstate pipelines conduct their production activities through producing divisions. To the extent that gas produced by a production division is mixed with gas purchased from others, Petitioners would deny NGPA prices to that production. This Court should not countenance a construction that would lead to absurd and unreasonable results and that would thwart the obvious purposes of the NGPA. *See Trans Alaska Pipeline Rate Cases*, 436 U.S. 631, 643 (1978); *United States v. American Trucking Ass'ns*, 310 U.S. 534, 543 (1940).

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[38] Under the Petitioners' interpretation, a further fragmentation of the market would result in states where intrastate pipelines are not regulated by state regulatory authorities. Those unregulated intrastate pipelines would be able to charge for their production whatever the market would bear. In the absence of state regulation, the only possible control over the price chargeable by these pipelines would be the Commission's authority under NGPA section 2(21)(A)(v). Even were the Commission to assert such control, the result would be "first sale" treatment of unregulated intrastate pipeline production, and state cost of service regulation over other intrastate pipeline production.

[39] The practical consequences which flow from the Petitioners' interpretation are detailed in a series of hypotheticals in Appendix C.

V. THE DECISION BELOW DOES NOT RESULT IN A "WINDFALL"

Petitioners contend that the decision below will result in "windfall" profits to pipeline companies whose production has previously been priced on a cost of service basis. (FERC Brief, at 13, 34-35; New York Brief, at 34-35.) Pipeline production that was subject to cost of service pricing on the date of the enactment of the NGPA was a small, rapidly-diminishing portion of total natural gas production.[40] As a consequence, the economic impact of the decision of the court below represents only a small fraction of the total impact of the NGPA.[41]

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[40] Department of Energy statistics demonstrate that approximately 95 percent of all gas dedicated to the major interstate pipelines in 1979 was provided by independent producers who are undeniably entitled to NGPA prices. *Energy Data Reports, Domestic Natural Gas Reserves And Production Dedicated To Interstate Pipeline Companies*, 1981, at 2 (Dept. of Energy, July 27, 1982.) The remaining 5 percent was owned by pipelines or their affiliates. By virtue of Order Nos. 58 and 98, however, a substantial portion of that 5 percent representing all production by pipeline affiliates and all new gas production by pipelines would have qualified for NGPA prices in the absence of the decision below. The volume of production directly affected by the decision below, therefore, is relatively small, and produced from older leases and from wells that are rapidly depleting.

[41] The economic impact of the decision below is illustrated in Appendix D. The bar graph reflects the following assumptions and conclusions to establish the *de minimis* impact of the *Mid Louisiana* decision on retroactive claims for NGPA 1979-81 and on the annual impact of that decision as measured in 1981: (1) In the absence of the NGPA, wellhead prices would have escalated through 1981 at the same average annual rate experienced for the five years before 1979 ($.138); (2) The total impact of the NGPA on total natural gas production would thus be approximately $24 billion for the period 1979-81; (3) Retroactive claims attributable to the *Mid Louisiana* decision for the period 1979-81 amount to $347 million, or 1.44 percent of the total NGPA impact for 1979-81; (4) The total annual impact of the NGPA for 1981 would be approximately $13 billion; (5) The claims attributable to the *Mid Louisiana* decision for 1981 amount to $181 million, or 1.37 percent of the total NGPA impact for 1981. The Appendix illustrates that the decision below has a relatively small dollar impact when compared with other applications of the NGPA which are uncontroverted. Petitioners' contentions of "windfall profits," therefore, belie economic reality.

All parties acknowledge that the NGPA dramatically altered the pricing system applicable to the more than ninety percent of total gas production attributable to independent producers or affiliates of pipelines and local distribution companies. The question before this Court is whether Congress intended to exempt from the alteration the small and declining volumes of pipeline production. The court below did not decide whether NGPA prices were appropriate as a matter of policy; it simply decided that the price structure designed by Congress was intended to apply to *all* domestic natural gas production.[42]

Cries of "windfall" profits were raised when the NGPA was before Congress. Congress balanced the competing economic interests by establishing a uniform pricing policy for all domestically-produced natural gas.[43] Peti-

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[42] It is well settled that courts do not substitute their social and economic beliefs for the judgment of legislative bodies. Ferguson v. Skrupa, 372 U.S. 726, 730 (1963). As this Court stated in a unanimous opinion in 1941, "We are not concerned . . . with the wisdom, need, or appropriateness of the legislation." Olsen v. Nebraska ex rel. Western Reference & Bond Ass'n, 313 U.S. 236, 246 (1941). *See also* Exxon Corp. v. Governor of Maryland, 437 U.S. 117, 124 (1978); American Commercial Lines, Inc. v. Louisville & Nashville R.R. Co., 392 U.S. 571, 590 (1968).

[43] As the Fifth Circuit observed in *Pennzoil Co. v. FERC*, "Congress carefully considered the economic impact of the NGPA in designing the Act." 645 F.2d 360, 379 n.37 (5th Cir. 1981), *cert. denied*, 454 U.S. 1142 (1982).

For example, Congress recognized that a special incentive rate was required to preserve production from marginal wells that produced small volumes, but that in the aggregate represented a significant resource, *i.e.*, "stripper wells." In delineating the criteria for qualification as a "stripper well," Congress did not distinguish among types of producers. NGPA § 108, 15 U.S.C. § 3318 (Supp. IV 1980). *See* 123 Cong. Rec. S15551, S15553, S15563 (daily ed. Sept. 24, 1977); *Stripper Well Natural Gas; Final Regulations and Amendments to Interim Regulations*, 44 Fed. Reg. 49,656 (Aug. 24, 1979). In fact, legislative efforts to limit the "stripper well" incentive pricing provisions to particular producers failed. *See* 123 Cong. Rec. S15550-51, S15559, S15562 (daily ed. Sept. 24, 1977); 123 Cong. Rec. S15608 (daily ed. Sept. 26, 1977).

tioners reargue the same positions that were considered and rejected by Congress when it enacted the NGPA. Petitioners' remedy is with Congress and not with this Court.

Petitioners also suggest that a "windfall" would result because pipeline companies that received cost of service pricing for their production bore no risk of loss.[44] At one time, all producers—whether independent or pipeline—received cost of service pricing for their production. Similarly, at a later point, *all* producers received area-wide or nationwide rates based upon what the Commission determined to be the average cost of exploration, development, and production of natural gas. Lease-acquisition costs, dry-hole costs inevitably incurred in the search for gas, and the costs of successful wells were included in the Commission's cost determinations upon which those area rates were based.[45] Under cost of service regulation, all that pipeline producers have the opportunity to recover are average costs, as determined by the Commission on the basis of subjective cost allocation techniques developed long after the costs were incurred. Thus, if it were possible to trace each production dollar from its expenditure to its recovery from consumers, it is likely that consumers did not pay for leases or wells owned by pipelines any more than they paid for leases or wells drilled by its affiliates, co-venturers, partners, or independent producers, although some pipeline production continued to be priced on a cost of service basis. In each instance, the consumer paid only an amount determined

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[44] AEPCO Brief, at 15, 16, 28, 29 & n.19; New York Brief, at 3, 28, 34; FERC Brief, at 5 & n.8, 33.

[45] *See, e.g.*, Opinion No. 468, Area Rate Proceeding (Permian Basin Area), 34 F.P.C. 159 (1965), *aff'd sub nom.* Permian Basin Area Rate Cases, 390 U.S. 747 (1968).

by the Commission to be "just and reasonable" under the Natural Gas Act.[46]

Petitioners' contention that gas consumers bore all of the risks of pipeline production ventures also ignores the fact that many pipeline producers acquired the production properties from which "old" gas is produced years before Congress enacted the NGA and well before the Commission announced that production must be priced on a cost

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[46] Cost of service pricing is never a guarantee of full cost recovery. Undeniably, cost-based regulation permits an interstate pipeline company the opportunity to recover some of the costs of production, including a utility-type return on investment. There is nothing to support the Petitioners' contentions, however, that pipelines have recovered, or will recover, *all* production costs under cost of service ratemaking and thus have no risk. Under the NGA, the Commission is empowered to prevent the recovery of costs under certain circumstances. *See* 15 U.S.C. § 717c(e) (1976); FPC v. Louisiana Power & Light Co., 406 U.S. 621, 645 (1972). In fact, the FERC has routinely adopted techniques in pipeline rate cases that prevent full-cost recovery, such as the averaging of exploration and development costs. *See, e.g.*, Southern Natural Gas Co., Opinion No. 379, 29 F.P.C. 323, 329-30 (1963); United Carbon Co., 25 F.P.C. 181, 187 (1961).

The recoupment of production costs under cost of service ratemaking depends greatly upon the timing of rate proceedings, the accuracy of test-period projections, the extent of regulatory lag, overall cost levels, and the FERC's treatment of particular rate issues, such as the recovery of unsuccessful exploration and development costs, including dry-hole expenses. For example, in Order No. 440, 46 F.P.C. 1148 (1971), the Commission permitted "full-cost accounting" for all exploration and development expenditures incurred on leases acquired on or after October 7, 1969 as opposed to the prior practice of expensing nonproductive well drilling and other costs. Such "full-cost accounting" permits a company to capitalize all exploration and development costs coupled with future write-offs against revenues from producing wells. Pipelines incurring exploration and development costs on leases acquired before October 7, 1969, on the other hand, must expense those costs and thus do not recover the full scope of the costs of production and exploration.

of service basis.[47] At that time, pipelines certainly could not predict the Commission's pricing policy.[48]

Petitioners' main concern appears to be the pipeline production that will qualify for section 108 prices.[49] Although it offers no factual support for its assertion, the FERC contends that most of the expenditures relating to old wells have already been made and "paid for by . . . consumers" and that "the operation of a well in its later

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[47] *See, e.g.*, Canadian River Gas Co. v. Pub. Serv. Comm., 3 F.P.C. 32 (1942); *aff'd sub nom.* Colorado Interstate Gas Co. v. FPC, 324 U.S. 581 (1945); Panhandle Eastern Pipe Line Co. v. FPC, 324 U.S. 635 (1945); Hope Natural Gas Co., 3 F.P.C. 150 (1942), *aff'd sub nom.* Federal Power Comm'n v. Hope Natural Gas Co., 320 U.S. 591 (1944).

[48] Petitioners also suggest, without support, that the average cost of service of pipeline production was approximately 26¢ per Mcf upon passage of the NGPA. (FERC Brief, at 34 n.35.) In Opinion No. 749, 54 F.P.C. 3090 (1975), the Commission found that the average national cost of service from such wells was 14.47¢ per Mcf and increased that rate by 8.73¢ so that flowing gas would bear part of the burden of the cost of new exploration and development. Similarly, it has been Consolidated's experience that its cost of service for gas production approximates that of independent producers operating in the Appalachian basin. Thus, it should profit no more from the receipt of NGPA prices than similarly situated independent producers.

[49] In its Brief, the FERC conjures up an example of pipelines receiving an additional $3.27 per MMBtu "pure profit" from stripper wells. (FERC Brief, at 34-35 n.35.) The older, rapidly-depleting wells that are the subject of Order No. 58 fall generally into two NGPA pricing categories—section 104 and section 108. Gas subject to section 104 pricing will continue to be priced at the just and reasonable rates in effect immediately preceding the NGPA, adjusted for inflation. This clearly provides no "windfall" to pipeline producers. The NGPA preserved cost-based regulation only to the limited extent provided in NGPA section 104. NGPA section 101(b)(9) provides, however, that if gas qualifies under more than one section, including section 104, producers may collect the highest price for which they qualify if contractually authorized. Thus, pipeline production may remain subject to cost of service pricing unless it qualifies for a higher price, such as the NGPA section 108 stripper well price.

years is relatively inexpensive." (FERC Brief, at 34 n.35.) This unsupported assertion fails on all counts. First, consumers pay a rate which reflects average pipeline costs, but the capital and operating expenditures are made by the pipeline's investors on a well-by-well basis, and they bear the risk of failure to recover fully those costs. Second, the *unit* costs of operating a well in its later years increase dramatically. As reserves underlying a producing well decline, production rates also decline, generally to a fraction of the rate experienced in the earlier years of production.[50] As a result, the remaining investment in the wells,[51] as well as operating costs,[52] must be recovered over much smaller production volumes. Frequently, to maintain production, wells must be reworked often at substantial expense.[53]

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[50] Typically, in the Appalachian area, over one-half of the reserves underlying a well are recovered in the first three or four years, and the remainder over a period of decades.

[51] Depreciation, depletion, and amortization charges (DD&A) are a significant component of the cost of producing gas. *See* Opinion No. 468, Area Rate Proceeding (Permian Basin Area), 34 F.P.C. 159 (1965), *aff'd sub nom.* Permian Basin Area Rate Cases, 390 U.S. 747 (1968).

[52] Operating costs include labor expenses necessary to monitor wells, metering, maintenance of the well, testing, cleaning well locations, repairing roads to well sites, painting equipment, and travel expenses to and from wells. These expenses do not vary with volume. Whether 1 MMBtu or 1000 MMBtu are produced, the well must be maintained and all of the expenses must be incurred.

[53] The FERC also blithely assumes that continued cost of service treatment is sufficient incentive for pipelines to engage in the enhanced recovery efforts necessary to recover more gas from old stripper wells as envisioned by Congress. (FERC Brief, at 34, 35 & n.35.) Section 108(b)(2) provides that producers can continue to collect the stripper well rate even if production increased above 60 Mcf per day if such increased recovery is the result of "the application of recognized enhanced recovery techniques." Cost of service pricing at a utility-type return does not offer pipelines a sufficient incentive to engage in often-risky, enhanced recovery techniques, particularly if they can earn higher returns from the drilling of new wells.

Congress enacted section 108 to assure that reserves available from older, high-cost wells would be fully recovered and made available to consumers. Because the stripper well price is far below the cost of new gas supplies, such as imported gas,[54] or synthetic gas,[55] the consumer benefits from the extended production life made possible by the section 108 price. The legislative decision to provide an incentive for continuing production from marginal wells benefits consumers to a greater extent than the cost-based approach urged by Petitioners that would inevitably lead to abandonment of high-cost wells and the substitution of higher cost alternatives.

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[54] The current price of imported gas is $4.94 per MMBtu at the connection at the Canadian border. *See* Petroleum Intelligence Weekly, at 4 (Oct. 18, 1982).

[55] The estimated cost of synthetic gas from the Great Plains Coal Gasification Project, for example, is $10 per MMBtu. *See* Great Plains Gasification Associates, 19 F.P.S. 5-540 (Nov. 21, 1979).

CONCLUSION

The decision below is completely consistent with the legislative decision to reverse forty years of failed cost of service regulation and should be affirmed.

Respectfully submitted,

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APPENDIX A

GLOSSARY OF TERMS USED IN APPLICATION OF NGPA TO THE NATURAL GAS INDUSTRY

DOWNSTREAM

Operations performed after those at a point of reference. On a gas pipeline, downstream denotes a location further removed from the source of supply. 8 WILLIAMS & MEYERS, OIL & GAS LAW, Manual of Terms (1982).

FIELD PRICE

Computed from the weighted average arms-length prices established by federally unregulated bargaining for similar gas in the field. *City of Detroit v. F.P.C.*, 230 F.2d 810, 813 (D.C. Cir. 1955).

INDEPENDENT PRODUCER

Any person who is engaged in the production or gathering of natural gas and who sells natural gas in interstate commerce for resale, but who is without corporate affiliation with an interstate gas pipeline company. 18 C.F.R. § 154.91(a) (1982); *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672, 675 (1954).

INTERSTATE PIPELINE

Any person engaged in natural gas transportation subject to the jurisdiction of the Commission under the Natural Gas Act. Section 2(15) of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3301(15) (Supp. IV 1980).

INTRASTATE PIPELINE

Any person engaged in natural gas transportation (not including gathering) which is not subject to the

jurisdiction of the Commission under the Natural Gas Act (other than any such pipeline which is not subject to the jurisdiction of the Commission solely by reason of section 1(c) of the Natural Gas Act). Section 2(16) of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3301(16) (Supp. IV 1980).

LOCAL DISTRIBUTION COMPANY

Any person, other than any interstate pipeline or any intrastate pipeline, engaged in the transportation, or local distribution, of natural gas and the sale of natural gas for ultimate consumption. Section 2(17) of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3301(17) (Supp. IV 1980).

OFF-SYSTEM GAS

Gas produced by pipeline companies and sold to other pipeline companies, at the wellhead. *See City of Chicago, Illinois v. FPC*, 458 F.2d 731, 733-34 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972). 8 WILLIAMS & MEYERS, OIL & GAS LAW, Manual of Terms (1982).

REWORKING

Work performed on a well after its completion to secure production where there has been none, restore production that has ceased, or increase production. 8 WILLIAMS & MEYERS, OIL & GAS LAW, Manual of Terms (1982) and adopted in *House v. Tidewater Oil Co.*, 219 So.2d 616 at 622-623 (La. App. 1969), *writ refused*, 253 La. 1081, 221 So.2d 516.

APPENDIX B

Henry M. Jackson, Wash., Chairman

Frank Church, Idaho	Clifford P. Hansen, Wyo.
J. Bennett Johnston, La.	Mark O. Hatfield, Oreg.
James Abourezk, S. Dak.	James A. McClure, Idaho
Floyd K. Haskyll, Colo.	Dewey F. Bartlett, Okla.
Dale Bumpers, Ark.	Lowell P. Weicker, Jr., Conn.
Wendell H. Ford, Ky.	Pete V. Domenici, N. Mex.
John A. Durkin, N.H.	Paul Laxalt, Nev.
Howard M. Metzenbaum, Ohio	
Spark M. Matsunaga, Hawaii	
Wendell R. Anderson, Minn.	
John Melcher, Mont.	

Grenville Carside, Staff Director and Counsel
Daniel A. Dreyfus, Deputy Staff Director for Legislation
D. Michael Harvey, Chief Counsel
W. O. Craft, Jr., Minority Counsel

UNITED STATES SENATE

COMMITTEE ON
ENERGY AND NATURAL RESOURCES

Washington, D.C. 20510

June 6, 1978

MEMORANDUM

To: Senate Conferees on Natural Gas

From: Senator Henry M. Jackson

Re: Remaining Natural Gas Conference Issues

At the May 24 Conference Committee meeting the staff was directed to meet to develop suggestions for resolving the remaining natural gas conference issues.

The enclosed agenda covers all of the natural gas conference issues that were not addressed by the compromise proposal. Both the House and Senate positions on each issue are summarized and a staff recommendation is included for each issue except natural gas storage facilities.

The agenda will be covered at the Conference Committee meeting on Wednesday, June 7, 1978 at 2:00 p.m. in Room 2123 Rayburn House Office Building.

Questions concerning the agenda should be addressed to Betsy Moler, Staff Counsel, at extension 40611.

I. Pipeline Regulation and Pass Through of Price Increases

A. Pass Through of Wellhead Price Increases by Interstate Pipelines

House Provision:

Guarantees that interstate pipelines may pass through costs of natural gas purchases if the price of the purchased natural gas does not exceed the ceiling price levels established under the legislation. Natural gas prices equal to or less than the applicable natural gas ceiling prices established under the legislation are deemed "just and reasonable" for purposes of the Natural Gas Act.

[Section 417(a) and (b) respectively amending sections 4(a) and 5(a) of the Natural Gas Act; pages 40-41.*]

Senate Provision:

Guarantees that interstate pipelines may pass through costs of new natural gas purchases if the price of the purchased natural gas does not exceed:

(1) in the case of natural gas sold from offshore Federal lands, the applicable ceiling prices; and

(2) in the case of sales between affiliated entities, the price received in comparable transactions by persons not affiliated with the pipeline.

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* Page references are to be Comparative Print, dated November 28, 1977.

[Sections 205 and 206 respectively amending sections 4(e) and 5(a) of the Natural Gas Act; pages 40-41.]

Staff Recommendation:

Adopt House provision until date of deregulation. Thereafter use Senate provision modified to read:

Guarantee that interstate pipelines may pass through costs of deregulated natural gas purchases. In the case of transactions between affiliates, guarantee pass through if the price of the purchased natural gas does not exceed the price received in comparable transactions by persons not affiliated with the pipeline in the case of sales between affiliated entities.

APPENDIX C

Hypothetical No. 1:

Facts: Interstate pipeline A and Independent Producer X are joint venturers in a natural gas producing well drilled on January 1, 1968, on acreage that was committed or dedicated to interstate commerce within the meaning of the NGPA. A and X each own a ½ interest in the production from the well. A and X share equally in the costs of drilling and producing the gas. Their cost of production is 68¢ per MMbtu. The natural gas produced from the well qualifies under NGPA § 107(c)(4) as natural gas produced from Devonian shale. X sells 100% of its ½ share of the production to A which commingles the gas purchased from X with his own gas from the joint venture well and with gas purchased from others. A then sells the entire gas stream to its four (4) system customers, one-fourth (¼) each.

Question No. 1: Is the natural gas production subject to the Commission's NGA jurisdiction?

Question No. 2: What prices will X and A receive for their respective ½ interests in the production?

The Petitioners' Answer: X's gas is not subject to the Commission's NGA jurisdiction due to NGPA § 601(a)(1)(B)(i) and X will receive a deregulated price if his contract contains a "renegotiation-in-the-event-of-deregulation" clause or if his contract expires in 1983 (many contracts are for fifteen-year terms). A's production is subject to the Commission's NGA jurisdiction, and A may receive only such amounts as the Commission, in its discretion, determines is "just and reasonable" under NGA section 4; which may be more or less than the deregulated price which X obtains.

Hypothetical No. 2:

Facts: Pipeline A owns a natural gas producing well. Pipeline A sells the production from that well in three

different ways: One-third of the production is sold at the wellhead to customer No. 1 who picks it up at the wellhead; one-third of the production is dedicated by contract to customer No. 2 who takes delivery of an equivalent volume of natural gas downstream, after the gas identified to the contract has been commingled by Pipeline A with natural gas purchased from others; one-third of the production is not identified to any particular customer, but is commingled with Pipeline A's purchased gas and sold downstream, along with the purchased gas, to customers No. 3 and No. 4.

Question No. 1: Which sales of the pipeline's production qualify as "first sales" under the definition of NGPA section 2(21)?

The Petitioners' Answer: Only the sales to customer Nos. 1 and 2.

Question No. 2: Does the answer depend upon whether the natural gas was previously priced under area-wide or nationwide rates or on a cost of service basis?

The Petitioners' Answer: No. Natural gas produced by a pipeline and sold as a part of system supply *never* becomes subject to NGPA pricing. However, the Commission may, in its discretion, choose to permit pipelines to charge prices equal to NGPA Title I prices if it determines that the price is just and reasonable under the NGA.

Question No. 3: What prices will A receive?

The Petitioners' Answer: Any NGPA price or deregulated price for which A may qualify under NGPA and contract for with customer Nos. 1 and 2; and only a price based upon A's cost of production plus a utility-type return with respect to the sales made to customer Nos. 3 and 4.

Hypothetical No. 3:

Facts: Interstate pipeline A and intrastate pipeline B are joint venturers in an onshore production well in state X which qualifies only under NGPA section 103. Both A and B lay separate gathering lines to the well, but both commingle their shares of the gas from the well with gas purchased from others prior to sale. A transports its gas into state Y and sells it and the other gas it has purchased to distribution companies C and D. Intrastate pipeline B transports its gas solely within state X and sells it to two industrial customers, E and F. State X does not regulate the price of intrastate pipeline sales if they sell gas only to end users and do not "distribute" gas to residential and commercial customers.

Question No. 1: What prices will A and B receive for their respective interests in the production from the well?

The Petitioners' Answer: In accordance with the Commission's exercise of discretion in Order 98, pipeline A will receive only the NGPA section 103 price plus transmission and storage costs which the Commission finds to be just and reasonable. In contrast, intrastate pipeline B will receive whatever the market will bear unless and until the Commission exercises its "discretion" to include mixed volume sales in the first sale definition of NGPA to "prevent circumvention", which may be long after the well is depleted.

APPENDIX D

ECONOMIC IMPACT OF THE MID LOUISIANA DECISION

Assuming wellhead prices escalate through 1981 at the same average annual rate experienced in the five years before 1979 ($.138/Mcf per year).

	1979	1980	1981	TOTAL 1979-81
AVERAGE WELLHEAD PRICE		($/Mcf)		
With NGPA	1.178	1.603	1.995 [1]	
Without NGPA	1.043	1.181	1.319 [2]	
TOTAL GAS INDUSTRY		VOLUMES (Bcf)		
Producer Purchases	19030	19017	18882	56929 [3]
Pipeline Production	633	585	524	1760 [4]
TOTAL	19663	19602	19424	58689 [5]

[1] Actual average wellhead value of natural gas produced in the United States. Energy Information Administration, *Monthly Energy Review*, DOE/EIA-0035, September, 1982.

[2] Assumed average wellhead value of natural gas produced without passage of the Natural Gas Policy Act. This price was determined by escalating the 1978 price, and each subsequent year, by the average annual rate increase for the five years before passage of the NGPA ($.138/Mcf per year). The actual annual increases were as follows:

	Increase
1974	$.088
1975	$.141
1976	$.135
1977	$.210
1978	$.155
Average	$.138

[3] Producer purchases determined by subtracting pipeline production identified at *infra* note 4 from total industry production identified at *infra* note 5.

[4] Pipeline production reported for 20 major interstate pipelines. Energy Information Administration, *An Analysis of Post-NGPA Interstate Pipeline Wellhead Purchases*, DOE/EIA-0357, September, 1982.

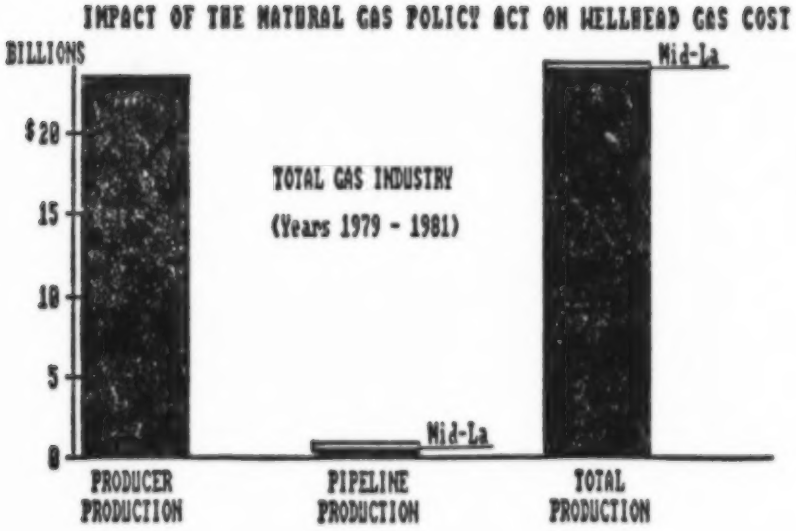
[5] Total net dry marketed production for the total industry. Energy Information Administration, *Monthly Energy Review*, DOE/EIA-0035, September, 1982.

	1979	1980	1981	TOTAL 1979-81	
TOTAL MID LA COMPANIES					
Producer Purchases	2116	2017	2068	6201 [6]	
Pipeline Production	456	431	390	1277 [7]	
TOTAL	2572	2448	2458	7478 [8]	
TOTAL GAS INDUSTRY	COST ($ Millions)				
Producer Purchases					
With NGPA	22417	30484	37670	90571	
Without NGPA	19848	22459	24905	67213	
NGPA Impact	2569	8025	12764	23358	
Mid La Retroactive Claims				347	
Ratio of Mid La Claims To Total NGPA Impact (1979-1981)				.014855	(347/23358)
Mid La Annual Amount			181		
Ratio of Mid La Claims To Total NGPA Impact (1981)			.014180		(181/12764)
Pipeline Production					
With NGPA	746	938	1081	2765	
Without NGPA	660	691	715	2066	
NGPA Impact	85	247	366	699	
Mid La Annual Amount				347	
Ratio of Mid La Claims To Total NGPA Impact (1979-1981)				.496625	(347/699)
Mid La Retroactive Claims			181		
Ratio of Mid La Claims To Total NGPA Impact (1981)			.494006		(181/366)
TOTAL GAS INDUSTRY					
With NGPA	23163	31422	38751	93336	
Without NGPA	20509	23150	25620	69279	
NGPA Impact	2654	8272	13131	24057	
Mid La Annual Amount				347	
Ratio of Mid La Claims To Total NGPA Impact (1979-1981)				.014424	(347/24057)
Mid La Retroactive Claims			181		
Ratio of Mid La Claims To Total NGPA Impact (1981)			.013785		(181/13131)

[6] Total volumes for (7) companies listed in Solicitor General's Reply Memorandum. Energy Information Administration, *An Analysis of Post-NGPA Interstate Pipeline Wellhead Purchases*, DOE/EIA-0357, September, 1982. (Excludes Kentucky-West Virginia and Mid Louisiana).

[7] *Id.*

[8] *Id.*


IMPACT OF THE NATURAL GAS POLICY ACT ON WELLHEAD GAS COST
BILLIONS
$20
15
10
5
0
TOTAL GAS INDUSTRY
(Years 1979 - 1981)
Mid-La
Mid-La
PRODUCER PRODUCTION
PIPELINE PRODUCTION
TOTAL PRODUCTION

Respondent's Brief

3

Supreme Court, U.S.
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Nos. 81-1889, 81-1958, 81-2042 and 82-19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*,
Petitioner,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

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BRIEF FOR RESPONDENT MICHIGAN WISCONSIN PIPE LINE COMPANY

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January 11, 1983

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

QUESTION PRESENTED

Did the Congress, when it substituted its own legislated price control system for natural gas, in place of the former system of controls by the Federal Energy Regulatory Commission, admittedly making the Congressional controls applicable to gas produced by "independent" producers of gas and producers which are affiliated with pipeline companies, make such controls applicable to only a very small part of the gas produced by pipeline companies, and thus carve out an exception for almost all gas produced by pipelines, all without any indication of such alleged exception in the statutory language or legislative history, and contrary to express statutory language. The Court of Appeals held that no such exception exists: that Congressional price controls apply to all natural gas produced in the nation.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
TABLE OF AUTHORITIES	v
STATEMENT OF THE CASE	1
1. The History And Purpose Of The NGPA	1
2. The FERC Orders Involved In This Proceeding	3
3. The Opinion Below	4
SUMMARY OF ARGUMENT	5
ARGUMENT	7
I. THE COURT BELOW CORRECTLY HELD THAT THE LANGUAGE, PURPOSE AND LEGISLATIVE HISTORY OF THE NGPA REQUIRE THAT THE NGPA PRICE SYSTEM APPLY TO ALL PIPELINE PRODUCED GAS	8
A. The Language Of The NGPA Requires The Interpretation Made By The Court Below	8
1. Section 2(21) Of The NGPA Requires The Decision Of The Court Below	8
2. Section 601(b)(1)(E) Of The NGPA Strongly Supports The Decision Of The Court Below	13
B. The Legislative History And Purposes Of The NGPA Strongly Support The Decision Below	18
II. THE COURT BELOW PROPERLY REJECTED THE CLAIMS OF PETITIONERS	24
A. The Interpretation Of The NGPA By The FERC Is Erroneous, Illogical And Discriminatory	25

TABLE OF CONTENTS—Continued

Page

B. The Decision Below Does Not Impede The Regulatory Duties Of The FERC Or The States 34

C. The Decision Below Is Correct, Irrespective Of Which Concept Of When The "First Sale" Takes Place Is Accepted 38

III. THE DECISION BELOW PRODUCES A JUSTIFIED RESULT 44

CONCLUSION 50

TABLE OF AUTHORITIES

Cases	Page
American Tobacco Co. v. *Patterson*, 102 S. Ct. 1534 (1982)	11
Arizona v. *California*, 373 U.S. 546 (1963)	24
Colorado Interstate Gas Co. v. *FPC*, 324 U.S. 581 (1945)	49
Consumer Product Safety Commission v. *GTE*, 447 U.S. 102 (1980)	18
Currin v. *Wallace*, 306 U.S. 1 (1939)	28
Dandridge v. *Williams*, 397 U.S. 471 (1970)	42
Davies Warehouse Co. v. *Bowles*, 321 U.S. 144 (1944)	32
Dawson Chemical Co. v. *Rohm & Haas*, 448 U.S. 176 (1980)	11
Espinoza v. *Farah Mfg.*, 414 U.S. 86 (1973)	32
Ex Parte Collett, 337 U.S. 55 (1949)	12
Federal Maritime Comm. v. *Seatrain Lines, Inc.*, 411 U.S. 726 (1973)	32
FPC v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944)	43
FTC v. *Colgate-Palmolive Co.*, 380 U.S. 374 (1965)	32
Hatch v. *Standard Oil Co.*, 100 U.S. 124 (1879)	44
Helvering v. *Lerner Stores*, 314 U.S. 463 (1941)	42
International Brotherhood of Teamsters, Chafeurs, Warehouseman and Helpers of America v. *Daniel*, 439 U.S. 551 (1979)	11, 32
Letulle v. *Scofield*, 308 U.S. 415 (1940)	42
Mohasco Corp. v. *Silver*, 447 U.S. 807 (1980)	32
Morton v. *Ruiz*, 415 U.S. 199 (1974)	32
Neuberger v. *Comm'r*, 311 U.S. 83 (1940)	32
NLRB v. *Brown*, 380 U.S. 278 (1965)	32
NLRB v. *Hearst Publications*, 322 U.S. 111 (1944)	39
Phillips Petroleum Co. v. *Wisconsin*, 347 U.S. 672 (1954)	1
Public Service Electric & Gas Co. v. *FPC*, 371 F.2d 1 (3rd Cir. 1967)	44
Reagan v. *Farmers Loan and Trust Company*, 154 U.S. 362 (1893)	28

TABLE OF AUTHORITIES—Continued

	Page
Rubin v. *U.S.*, 449 U.S. 424 (1981)	18
Ryerson v. *U.S.*, 312 U.S. 405 (1941)	42
Schneider v. *Rusk*, 377 U.S. 163 (1964)	28
SEC v. *Sloan*, 436 U.S. 103 (1978)	32
Shea v. *Vialpando*, 416 U.S. 251 (1974)	32
United Gas Improvement Co. v. *Continental Oil Co.*, 381 U.S. 392 (1965)	39
United States v. *American Railway Express*, 265 U.S. 425 (1924)	42
United States v. *New York Telephone Co.*, 434 U.S. 159 (1977)	42
United States Department of Agriculture v. *Moreno*, 413 U.S. 528 (1973)	27
Usery v. *First National Bank of Arizona*, 586 F.2d 107 (9th Cir. 1978)	32
Volkswagenwerk Aktierge v. *Fed. Mar. Comm.*, 390 U.S. 261 (1968)	32

Statutes

Natural Gas Act, 15 U.S.C. §§ 717, *et seq.*	*passim*
§ 4e (15 U.S.C. § 717(c) (e)	15
§ 5a (15 U.S.C. § 717(d) (a))	15
Natural Gas Policy Act of 1978, 15 U.S.C. 3301, *et seq.*	*passim*
§ 2(20) (15 U.S.C. 3301(20))	40
§ 2(21) (15 U.S.C. 3301(21))	*passim*
§ 2(22) (15 U.S.C. 3301(22))	44
§ 101 (15 U.S.C. 3311)	2, 3, 11
§ 102 (15 U.S.C. 3312)	2, 3, 11
§ 103 (15 U.S.C. 3313)	2, 3, 11
§ 104 (15 U.S.C. 3314)	2, 3, 11, 46
§ 105 (15 U.S.C. 3315)	2, 3, 11
§ 106 (15 U.S.C. 3316)	2, 3, 11
§ 107 (15 U.S.C. 3317)	2, 3, 11
§ 108 (15 U.S.C. 3318)	2, 3, 11
§ 109 (15 U.S.C. 3319)	2, 3, 11
§ 110 (15 U.S.C. 3320)	43
§ 121 (15 U.S.C. 3331)	2
§ 122 (15 U.S.C. 3332)	2

TABLE OF AUTHORITIES—Continued

	Page
§ 201 (15 U.S.C. 3341)	2
§ 202 (15 U.S.C. 3342)	2
§ 203 (15 U.S.C. 3343)	2, 18, 24
§ 204 (15 U.S.C. 3344)	2
§ 205 (15 U.S.C. 3345)	2
§ 206 (15 U.S.C. 3346)	2
§ 207 (15 U.S.C. 3347)	2
§ 208 (15 U.S.C. 3348)	2
§ 311 (15 U.S.C. 3371)	2
§ 315 (15 U.S.C. 3375)	17
§ 401 (15 U.S.C. 3391)	2
§ 402 (15 U.S.C. 3392)	2
§ 403 (15 U.S.C. 3393)	2
§ 404 (15 U.S.C. 3394)	2
§ 601(a) (15 U.S.C. 3431(a))	2, 37
§ 601(b)(1)(E) (15 U.S.C. 3431(b)(1)(E))	*passim*
§ 601(c) (15 U.S.C. 3431(c))	13
§ 602(a) (15 U.S.C. 3432(a))	36
Administrative Procedure Act, 5 U.S.C. § 500 *et seq.*	28
5 U.S.C. 706(2)(A)	28
5 U.S.C. 706(2)(B)	28
5 U.S.C. 706(2)(C)	28

Legislative History References and Texts

Staff of Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 2d Sess., "Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978" (Comm. Print 62)	21
124 Cong. Rec. H13114 (daily ed. Oct. 14, 1978)	22, 23
124 Cong. Rec. H13118 (daily ed. Oct. 14, 1978)	22
H.R. Conf. Rep. No. 1752, 95th Cong., 2d Sess. (1978)	22, 41
S. Rep. No. 436, 95th Cong., 1st Sess. (1977)	22
S. 2104, 95th Cong., 1st Sess. (1977), as passed by the Senate on Oct. 4, 1977, 123 Cong. Rec. S16325	15, 16

TABLE OF AUTHORITIES—Continued

Page

S. Rep. No. 43, 96th Cong., 1st Sess. (1979) 21

Hearings on H.R. 6831, *et al.*, Before the Subcommittee on Energy and Power of the House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess., ser 23, Pt. 2 (1977) 23

A. Sutherland, *Statutory Construction*, Section 46.01 (4th Ed. 1973) 12

67 Am. Jur. 2d Sales § 6 44

U.C.C. § 2-106 44

U.C.C. § 2-107 44

U.C.C. § 2-401 44

Opinions and Orders of the FERC

Interim Regulations Implementing the NGPA of 1978, Docket No. RM79-3, 43 Fed. Reg. 56448 (Dec. 1, 1978) 32, 33

Order No. 58, Final Rule Covering the Maximum Lawful Price for Pipeline Distributor and Affiliate Production, Docket No. RM80-7 (Nov. 14, 1979), 43 Fed. Reg. 66577 (Nov. 20, 1979) ..... *passim*

Order No. 98, Final Rule Governing Pricing of Pipeline Production Under the Natural Gas Act, Docket No. RM80-6 (Aug. 4, 1980), 45 Fed. Reg. 53091 (Aug. 11, 1980) 5, 33, 45

Order No. 102, Order Denying Rehearing of Order No. 58 and Order No. 98 and Clarifying Order No. 98, Docket Nos. RM-6 and RM80-7 (Oct. 3, 1980) 13 FERC ¶ 61,013 1

Opinion No. 568, Pipeline Production Area Rate Proceeding (Phase I), Docket No. RP66-24, 42 F.P.C. 738 (1969), *reh. den.* 42 F.P.C. 1089 (1969) 21

Opinion No. 47, *Columbia Gulf Transmission Co., et al.*, Docket No. RP75-105, *et al.* 8 FERC ¶ —— (July 2, 1979) 21

Canadian River Gas Co., et al., 3 F.P.C. 32 (1942), *aff'd sub nom., Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945) 49

TABLE OF AUTHORITIES—Continued

Page

Cities Service Gas Co., 39 F.P.C. 1034 (1968) 49
National Fuel Gas Supply Corp., Opinion No. 58, F.P.C. Docket No. RP76-96, *et al.*, 18 F.P.S. 5-829 (1979) 48

Regulations of the FERC

18 C.F.R. § 2.76 46
18 C.F.R. § 2.77 46
18 C.F.R. § 270.203 28
18 C.F.R. § 270.203(a) 26
18 C.F.R. § 270.203(b) 26

BRIEF OF RESPONDENT MICHIGAN WISCONSIN PIPE LINE COMPANY *

STATEMENT OF THE CASE

This case involves the interpretation of the definition of the term "first sale" in Section 2(21) of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. § 3301(21). The Court below (664 F.2d 530), determined that the Federal Energy Regulatory Commission's (FERC)[1] interpretation of "first sale"[2] is inconsistent with the plain language of the NGPA and the clear intent of Congress in enacting the NGPA, and produces irrational, undesirable results.

1. The History And Purpose Of The NGPA

The basic purpose of the NGPA was to eliminate the national gas shortage by establishing a uniform national natural gas pricing policy, in order to stimulate the production of natural gas by legislative mandate of increased allowable prices to *all* producers of gas (both interstate and intrastate, so as to also eliminate the former intrastate advantage).

Before the NGPA, since *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954), the price for natural gas sold in *interstate* commerce, by all producers of natural gas, was determined by the FERC under the Natural Gas Act of 1938 (NGA), 15 U.S.C. §§ 717, *et seq.* The FERC first regulated all producer prices on a company by company basis, using a "cost of service" approach, but later began using "group" rates (first "area," and later, "national" rates) for all producers, including for all "new" pipeline produced gas. The pricing of *intrastate*

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* Pursuant to Rule 34.2, Respondents adopt those portions of the Brief filed by Petitioner Federal Energy Regulatory Commission (FERC) which are referred to in Rule 34(b), (d), (e) and (f). All appendix citations herein refer to the appendix filed by Petitioner, Public Service Commission of the State of New York in No. 81-1889.

[1] Both the FERC and its predecessor, the Federal Power Commission, are referred to herein as the "FERC".

[2] In Order Nos. 58 and 102 (App. B-1 and B-50).

gas, however, was *not* subject to the NGA or any other federal pricing regulation. With the passage of the NGPA, the above pattern totally changed. First, contrary to decades of past practice and law, the price control provisions of the NGPA bring *intrastate* natural gas under federal regulation provisions for the first time. Second, the NGPA wholly changed the basic pattern of price controls over natural gas, including total elimination of governmental price controls over certain categories of natural gas.[3] For categories of gas which remain subject to governmental price controls, temporarily or permanently, Congressionally established "maximum lawful prices" have replaced FERC discretion.[4]

The FERC continues to regulate the rates pipelines can charge for transporting and selling gas, but the "gas cost component" of pipeline rates is subject to NGPA price ceilings, not FERC fixed prices.[5]

The NGPA also created other far reaching statutory innovations for the natural gas industry and its regulation, including such matters as mandatory "incremental pricing", advance general authorization of approval of certain transactions between interstate and intrastate gas companies, establishment of certain natural gas service curtailment policies, and exclusion of certain transactions from FERC jurisdiction.[6] It is in the context of such

---

[3] See NGPA, Section 121 (15 U.S.C. § 3331).

[4] See NGPA, Sections 101 through 109 (15 U.S.C. §§ 3311 through 3319). The discretionary power to reinstitute price controls over certain categories of gas which will, under the NGPA, become decontrolled, was given to the President and Congress, not the FERC. See NGPA, Section 122 (15 U.S.C. § 3332).

[5] The prescribed prices for the gas *produced or purchased* by pipeline companies were, before the NGPA, fixed by the FERC, and were used by the FERC as the "gas cost component" of the overall pipeline "cost of service" which the FERC computed—and still computes—in order to calculate the rates which the pipelines may charge for their sales of gas. (See Section II B, below)

[6] See NGPA, Title II, Sections 201 through 208 (15 U.S.C. §§ 3341 through 3348); Section 311 (15 U.S.C. § 3371); Sections 401 through 404 (15 U.S.C. §§ 3391 through 3394); and Section 601(a) (15 U.S.C. § 3431(a)).

dramatic, far reaching Congressional changes in natural gas regulation that the narrow question presented herein arises.

2. The FERC Orders Involved In This Proceeding

About ninety-seven percent of natural gas which is sold by interstate pipelines is purchased from independent (non-affiliated) producing companies, and from separate producing companies which are affiliated with the pipeline company ("independent producers" and "affiliated producers," respectively). This proceeding does *not* involve such gas, since the FERC admits that NGPA prices apply to that gas. Rather, this proceeding involves *only* the pricing of a small part of the quite small portion of natural gas which is *produced by* interstate natural gas pipeline companies and sold to their customers.[7]

The pricing provisions of the NGPA fix a "maximum lawful price" for each category of *gas*, without mention of the producer thereof:[8] no distinctions are made which relate to the identity or corporate form of the producer. But the FERC, by Order No. 58 (App. B-1), has issued a regulation relative only to "maximum lawful prices" for gas produced by interstate pipelines, in which the FERC claims that despite the general removal of FERC pricing authority by the NGPA, the FERC has the authority to hold pipeline produced gas at prices other than those prescribed in the NGPA (and that states can totally ignore Federal controls, for gas produced by intrastate pipelines and distributors, but not for intrastate gas pro-

[7] Only a small fraction of pipeline produced gas is actually affected by this case, because of FERC action. See Section III hereof. The principles established by the Decision below would also affect gas produced by intrastate pipelines and distributors, as well as interstate pipelines, but reference is made mainly herein to the latter, because the FERC regulates only interstate pipelines, such as Respondents.

[8] See NGPA, Sections 101 through 109 (15 U.S.C. § 3311 through 3319). The prices are a stated base price and a method for adjusting it periodically, or an adoption of a prior fixed price, by reference, plus a method for adjustment.

duced by independent and affiliate producers). Further, the FERC has also claimed the power to pick and choose which *pipeline produced* gas would receive NGPA prices and which would not.[9] Inconsistently, Order No. 58 correctly interpreted the NGPA pricing provisions to apply to all gas produced and sold by producing companies which are *affiliates* of interstate pipelines, just as it does to independent producers. The NGPA makes no distinction between gas produced by "affiliated producers" and gas produced by the pipeline itself.

The FERC concedes that under its interpretation, the only pipeline produced gas which will be the subject of a "first sale" (and thus subject to NGPA pricing controls) will be that *extremely small* portion of such natural gas which is never "commingled" in a pipeline with natural gas purchased by the interstate pipeline company from other sources. But the language of the NGPA does not state, or indicate, any such distinctions within the category of pipeline produced gas, nor does it give the FERC authority to make such distinctions. As will be fully demonstrated below, such interpretation not only has no support in the plain meaning of the statute or the legislative history or purpose of the statute, but also makes no sense.

3. The Opinion Below

The Court of Appeals rejected the FERC's interpretation of "first sale", and the FERC's other efforts to maintain its pricing authority over pipeline produced gas. The Court held such efforts insupportable, in the face of the clear language and intent of the NGPA to replace FERC price controls with Congressional price controls for *all* natural gas, to eliminate interstate-intrastate disparities and to provide higher prices for produced gas. 664 F.2d at 535. Petitioners contend that by rules issued subse-

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[9] The FERC admits, in both Order No. 58 (App. B-3, 19) and its brief here (p. 30), that its interpretation of the NGPA would make almost no pipeline produced gas subject to NGPA price controls. New York's Brief, at 21, makes a similar admission.

quent to the Order here under review,[10] the FERC has provided a "better" pricing scheme for gas produced by interstate pipelines than the uniform pricing program which is provided in the statute. The Court of Appeals held such violation of the NGPA to be beyond the FERC's authority.

SUMMARY OF ARGUMENT

The Decision below held that pipeline companies have been authorized, by the NGPA, to include in their costs of service (and thus their rates), as the value for gas which they produce themselves, amounts equal to NGPA price ceilings, or such lower price as is reflected in comparable sales between non-affiliates. That is all that the pipelines ask: parity with affiliated producers, and a somewhat less favored status than independent producers.

The Court below correctly held that such parity is required by the express language, as well as the purposes and legislative history, of the NGPA. The direct language is the definition of "first sale" in Section 2(21) of the NGPA, where Congress expressly made the NGPA pricing system applicable to *all* natural gas produced, including all gas produced by pipeline companies. Section 601(b)(1)(E) of the NGPA supports that interpretation, since it covers "first sales" by pipelines and limits the values which pipelines may include in their costs of service, for gas which they produce, to the *lower* of NGPA prices *or* prices paid in sales between non-affiliates for comparable gas. That section thus provides to the consumer, regulatory protection against higher than mar-

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[10] In its Order No. 98 (App. B-14) the FERC, claiming that the NGPA does not apply NGPA pricing provisions to all gas, "granted" NGPA prices to some pipeline produced gas and denied it to other such gas. Petitioner Arizona Electric Power Cooperative, Inc. urges that if this Court affirms the Court below, it should nevertheless reverse as to the disposition of Order No. 98. But that is in error since, as the Court below properly held, Order No. 98 is based upon, and has meaning only in light of, the assumption that the FERC has power to deny "first sale" treatment to some gas. It does not, as shown herein.

ket values for pipeline produced gas, to supplement the restraints imposed by market conditions. The legislative history of the NGPA supports the concept that all pipeline production is the subject of a "first sale", and thus subject to NGPA pricing, and shows a clear Congressional desire to abandon FERC cost based regulation for the pricing of produced gas, and to encourage gas production by pipelines.

Petitioners claim that it is required that the language and legislative history specifically state that FERC authority to regulate pipeline produced gas has been set aside. In fact, that is what the NGPA does do, since it overthrows the FERC power to fix the price limits for *all* gas, which *includes* gas produced by pipelines. The Congressional aim was to undo the conditions which led to the gas shortages of the 1970's. Removal of FERC power over pipeline production was not nearly as substantial a change in prior law and practice as was the NGPA's extension of federal price controls to intrastate gas, its removal of FERC control over prices for the huge volume of gas produced by independent producers and producers affiliated with pipelines, and several other sweeping revisions of prior law and practice: the change as to pipelines was simply a relatively minor and consistent part of the new overall pattern. There was no reluctance evidenced by the Congress to change prior FERC practice in many areas: that is the major reason why the NGPA was enacted.

The FERC efforts to salvage some of its authority over pipeline produced gas requires the FERC to claim that various major portions of the NGPA were drafted in a way which is inconsistent with the statutory language and legislative history, are illogical, and were included for almost no reason. The FERC interpretation also produces invalid discrimination and classifications, based solely on corporate form. The language of the NGPA, however, does not make such distinctions. The FERC interpretation of "first sale" requires reading the word "attributable" as if it says, instead, "comprised exclusively of gas from identifiable wells, properties, or reser-

voirs," which is a tortured interpretation. The FERC interpretation also produces different price ceilings based upon irrelevant factors. Further, the Court below correctly held that its decision will prevent the intrastate-interstate disparities which the NGPA was intended to correct and which the FERC decision would create, as to pipeline and distributor produced gas. The Decision below also will not create any administrative burden or interference for FERC or state regulation of interstate pipelines, and intrastate pipelines and distributors, respectively. The controversy created by Petitioners over the place that the "first sales" of pipeline produced gas takes place is illusory: the result will be the same under each concept and the Court below can and should be affirmed on either concept.

Petitioners' claim that pipelines *should not* be able to receive NGPA prices for gas from their leases which were at any time regulated on a cost of service basis, lest a "windfall" come to pipelines, and disaster to the economy, is inaccurate, irrelevant, and an attempt to reargue past Congressional decisions.

Finally, the economic effects of the Decision below are small, relative to the overall effects of the NGPA, but nevertheless are a productive part of efforts to assure adequate gas supply to the nation.

ARGUMENT

The Decision below rejects the FERC effort to retain authority to apply whatever price regulation method it wishes to choose, to almost all natural gas produced by pipeline companies. The FERC interpretation would also leave states free to allow prices for gas produced by distributors and intrastate pipelines which are in excess of the NGPA maximum prices. Those results are in violation of the NGPA, which, for all gas, is designed and phrased to substitute Congressional price controls in place of the previous FERC regulation, and to apply Congressional ceilings to intrastate prices. The Court of Appeals correctly found that the language and legislative history

of the NGPA neither created, nor allows, such exceptions to the new Congressional price control program of the NGPA.

I. THE COURT BELOW CORRECTLY HELD THAT THE LANGUAGE, PURPOSE AND LEGISLATIVE HISTORY OF THE NGPA REQUIRE THAT THE NGPA PRICE SYSTEM APPLY TO ALL PIPELINE PRODUCED GAS

The directly relevant language of Section 2(21) explicitly makes the NGPA price control provisions applicable to all gas produced by pipelines. No exceptions are stated, or otherwise indicated. Thus, that provision alone is sufficient to affirm the Court of Appeals. In addition, however, other provisions of the Act, and the limited relevant legislative history, also support that conclusion.

A. The Language Of The NGPA Requires The Interpretation Made By The Court Below

1. *Section 2(21) Of The NGPA Requires The Decision Of The Court Below*

In the natural gas industry, the predominant pattern is that the first sale of gas is when an independent or affiliate producer of gas sells the gas to a pipeline company (which in turn sells it to a distribution company, in a second sale, or resale; the distributor then sells the gas to the consumer). In some cases, the pipeline itself produces the gas and first sells it to a consumer, or to the distributor, which resells to the consumer. In a few cases, the distributor produces the gas and first sells to the consumer. Consumer production is the exception. The NGPA makes the "first sale" of gas an event of basic regulatory significance, because the NGPA provides that the "maximum lawful prices" which are specified in each pricing section "shall apply to the first sale of" the natural gas categorized in the section. The NGPA also deregulates certain "first sales". The term "first sale" is defined in Section 2(21) of the NGPA, beginning with the following "general rule" of paragraph A:

(A) General Rule—The term "first sale" means any sale of any volume of natural gas—

(i) to any interstate pipeline or intrastate pipeline;

(ii) to any local distribution company;

(iii) to any person for use by such person;

(iv) which precedes any sale described in clauses (i), (ii), or (iii); and

(v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this Act.

That provision thus includes, as a first sale, the sales described above: to pipelines (A)(i), to distributors (A)(ii), and to consumers (A)(iii).[11] And that includes all of the types of sales which are made by pipelines: to other pipelines, to distributors and to users. It is *purchasers* which are defined: there is no exclusion of, or distinction as to, categories of *gas* or categories of *sellers*. However, since Section 2(21) is a definition of the "first sale" of the gas, the definition above would not be complete if the above provision were all there is, because the *first* sale of gas is made by the *producer* of the gas, and the purpose of the NGPA is to change and prescribe *producer* prices. Thus, the Section 2(21) definition of "first sale" also includes a Subsection (B), which states:

(B) Certain Sales Not Included—Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall *not* include the sale of any volume of natural gas *by* any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, *unless such sale is attributable to volumes of natural gas pro-*

[11] Subsections (A)(iv) and (A)(v) provide mechanisms so that the "first sale" definition, and thus NGPA price controls, *will apply* even if atypical first sales are created by gas sellers to try to avoid such controls. Ironically, the FERC attempts to twist the definition so that *it* will not be bound by the statutory controls, and to *deny* first sale status, which the NGPA does not allow the FERC to do.

> *duced by such interstate pipeline*, intrastate pipeline, or local distribution company, *or any affiliate thereof.* (emphasis added)

The *first* portion of that passage, which precedes the "unless clause", says that the sales described in the "General Rule" in Subsection A of Section 2(21)—which describes which entities the sales must be made *to*—shall *not* include sales *by* pipelines or distributors or their affiliates. That *exclusion* (which would go too far, but for the "unless clause") leaves the "general rule" covering sales *by producers* of gas *to* pipelines, distributors and users, as the statute is intended to do. And all gas is covered, *by* whomever produced, but only once. Section 2(21) also confines the definition to *first* sales, as intended. This is necessary not just to confine it to sales by producers, but also to avoid having the second or third sales of the same gas be additional "first sales". This is necessary because the NGPA is not intended to control such *resales* of gas by pipelines or distributors of gas which they *purchase*: the NGPA does not change the previously existing control by the FERC under the NGA over interstate pipeline *resale* rates for gas they *purchase*, nor of state control of intrastate pipeline and distributor *resale* rates for gas *they purchase*. The first clause of Subsection (B) avoids the unworkable result of more than one "first sale," relative to the same gas, by excluding sales of gas *by* pipelines, distributors and their affiliates, thus leaving sales of gas *by the producer to* a pipeline, to a distributor or to a consumer, as "first sales". There is thus *one* "first sale" of *all* gas: the sale by the producer of the gas.

However, Congress recognized that the first clause of Subsection (B) would also have eliminated from the "first sale" definition, the gas *produced* and *first* sold *by* pipelines, distributors and their affiliates. As to that gas, there would be *no* "first sale". To avoid that result, Congress added the "unless clause" in Subsection (B), so that, in totality, that subsection provides that a sale *by* a pipeline or distributor or affiliate is not a "first sale":

> *unless* such sale is attributable to volumes of natural gas *produced by such interstate pipeline*, intrastate pipeline, or local distribution company, *or any affiliate thereof.* (emphasis added)

Thus, it is clear that the gas sold by a pipeline (or distributor or affiliate) which has been produced by that seller (as opposed to having been purchased from a producer and resold) *is* the subject of a "first sale", and is thus subject to the applicable NGPA prices. This is because gas sold by a pipeline seller is not the subject of a "first sale", *unless* the gas was produced by the pipeline seller. If Congress had wished to leave gas produced by pipelines and distributors to FERC control, as the FERC contends it did, it could have simply left out the "unless clause". But it did not do so. As the Court of Appeals aptly stated: "Sections 3311-3319 of the NGPA set a price for the 'first sale' of natural gas in defined categories. Section 3301(21)(B) provides: (i) the sale of gas by a pipeline is not a 'first sale,' (ii) unless the sale was attributable to the pipeline's own production." 664 F.2d at 535.[12] The Decision below also explained that the "Commission's interpretation of section 3301 (21)(B) would effectively read the second part of this subsection out of the NGPA. By over-stressing the first provision that sales by a pipeline are not first sales, the Commission would render the unless clause of subsection (B) a nullity." 664 F.2d at 535.

The Court of Appeals' reading of the statute creates a logical pattern: (i) *All* gas produced by a pipeline *is* the subject of a "first sale", when *first* sold, and thus is subject to NGPA prices, and (ii) all gas produced by separate producing companies, which is the subject of a "first

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[12] The Court of Appeals reached that conclusion after noting (664 F.2d at 535) that "The starting point in every case involving the construction of a statute is the language itself." International Brotherhood of Teamsters v. Daniel, 439 U.S. at 558, 99 S.Ct. at 795 (1979). *See also* American Tobacco Co. v. Patterson, 102 S. Ct. 1534, 1537 (1982), Dawson Chemical Co. v. Rohm & Haas, 448 U.S. 176, 187 (1980).

sale" when sold by such companies to a pipeline or distributor or user (which is, in fact, the *first* sale of such gas), is *not* the subject of a "first sale" when *resold* by the pipeline or distributor (in a second or subsequent sale), so there are not two sales under the same price controls.

In contrast, the FERC's interpretation of the explicit definition of "first sale" in Section 2(21) would find that almost all pipeline produced gas is *not* the subject of *any* first sale: if that were correct, it would be the only domestic gas so excluded—and all without the statute or legislative history so stating. That reading would give the FERC authority to deviate from the logical regulatory pattern of the Act. The FERC holding, that it *can* deny NGPA pricing to almost all gas produced by pipelines, is in error: the FERC has *no* discretion to deny NGPA pricing to gas produced by pipelines, because it cannot change the express definition of "first sale" provided by the Congress in Section 2(21). The fundamental rule of statutory construction is that the plain meaning of the statute controls.[13]

The Decision below gives full meaning to all parts of Section 2(21), including the fact that neither the "unless clause", nor any other portion of Section 2(21), excludes pipeline produced gas or in any way differentiates between types of gas produced by pipelines (or other producers). Instead, *all* gas is the subject of *one* "first sale." The Court of Appeals' interpretation makes sense of the statute. The "unless clause" is necessary to, and serves to, preserve the symmetry of the statute, to make *all* gas, including *all* pipeline produced gas, the subject of one "first sale," but only one. As the Court of Appeals stated:

> Nothing in the language used here or elsewhere in the NGPA suggests any intent to deny NGPA pricing to natural gas just because it is produced by a pipeline. To the contrary, the unless clause of sub-

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[13] Ex parte Collett, 337 U.S. 55 (1949); *See*, 2A, A. Sutherland, Statutory Construction, Section 46.01 (4th ed. 1973).

> section (B) can only have meaning if it is interpreted as granting "first sale" status to gas which is attributable to pipeline production. 664 F.2d at 535.

The Court of Appeals' statutory interpretation does not create the distorted reading which the FERC's Order requires; it avoids reading distinctions into the NGPA which do not exist. It also avoids the FERC's discriminations, based on corporate form only, as between pipelines and their affiliate producers, as explained below. In short, the Court of Appeals reached the result which is required by the directly relevant language of the NGPA.[14]

2. *Section 601(b)(1)(E) Of The NGPA Strongly Supports The Decision Of The Court Below*

The provisions of Section 601(b)(1)(E) of the NGPA, 15 U.S.C. § 3431(b)(1)(E) provides further evidence that pipeline produced gas, like all other gas, is to be the subject of a first sale. In addition, that provision also disproves the claim of Petitioners that pipelines would be put into a preferred position relative to other producers by the Decision below. The provisions of Sections 601(b) and (c) of the NGPA, 15 U.S.C. § 3431(b) and (c), provide that the producer prices, and some other charges, specified in the NGPA, shall be deemed "just and reasonable", so that the FERC must allow pipelines to include in their costs of service, their costs resulting from such prices. However, the sale of gas by a producer to a pipeline with which it is affiliated, or by a pipeline to an affiliated distributor, and the inclusion, in a pipeline's cost of

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[14] The FERC and other Petitioners claim that the FERC's past freedom to choose the method for pricing gas produced by pipelines has been "repealed by *implication*" under the Decision below. In fact, however, that Decision correctly found that the NGPA *explicitly* removed that freedom, *just as it explicitly removed the FERC's freedom to control the price of gas sold by all other producers*, by the definition of "first sale" and the pricing provisions of the NGPA. Such result substitutes Congressional price ceilings for FERC prices, relative to the gas itself, by whomever produced, but leaves the FERC and state regulators with their long standing authority as to *resale* rates.

service, of an allowed price under the NGPA for gas produced by the pipeline, do not involve arms length bargaining or contracts. In contrast, an *independent* producer's arms length sales contract could result in negotiated limitations on price, in addition to the NGPA price controls. Accordingly, Congress provided a substitute for arms length bargaining, in Section 601(b)(1)(E), which provides:

> Affiliated entities limitation.—For purposes of paragraph (1), in the case of any *first sale between any interstate pipeline* and any affiliate of such pipeline, any amount paid in any *first sale* shall be deemed to be just and reasonable if, in addition to satisfying the requirements of such paragraph, such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline (emphasis added).

That Section thus provides that in addition to fitting within NGPA prices, the values assigned to gas produced and sold by pipelines, and their *affiliate* producers, must not exceed the prices in comparable first sales between non-affiliates. Thus, rather than being advantaged, pipelines and their affiliates are subject to price restrictions which they cannot control: the results of sales involving non-affiliates.[15]

Petitioners make the claim that Section 601(b)(1)(E) applies only to sales *by* affiliated producers *to* their affiliated pipeline, and does not cover sales *by* pipelines. But that is not what the statute says, and that contention is disproved by the legislative history. As to the statutory language, note that the Section does *not* say "in the case of any first sale *by* an affiliate of an interstate pipeline *to* such pipeline." Instead, it refers to a "sale *between* any interstate pipeline and any affiliate of such pipeline". Between is a "two-way" term, and makes clear that the

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[15] In addition, of course, pipelines and their affiliates, like non-affiliate sellers, are subject to market forces: concern that if their rates rise, they and their customers will lose sales. This is especially compelling in the current period.

Section covers not only "first sales" to the pipelines, by their affiliated producers, but *also* sales *by* the pipelines of the gas which they produce themselves. Both of those situations are functional equivalents, because they do not involve unrelated parties. They thus are treated the same way in Section 601, as well as in Section 2(21).

The legislative history further dispels any doubt as to whether the "affiliated entities limitation" was intended to cover pipeline produced gas. In June, 1978, conferees met to meld House and Senate bills into the legislation which became the NGPA. Sections 205 and 206 of the Senate Bill [16] would have amended Sections 4(e) and 5(a) of the Natural Gas Act (15 U.S.C. 717c(e) and 717d(a)), to each provide that the FERC could not prevent recovery by a pipeline in its rates, of NGPA price related costs, except:

> (B) in any case where a natural-gas company which transports natural gas in interstate commerce purchases new natural gas from an affiliate *or produces new natural gas from its own properties*, to the extent that the Commission determines that the rates and charges therefor exceed the current rates and charges, or portion thereof, made, demanded, or received for comparable sales by persons not affiliated with such natural-gas company. (emphasis added)

That language shows that the Senate Bill was intended to apply the comparable price between non-affiliates, "affiliated entities limitation", which is now in Section 601(b)(1)(E) of the NGPA, to gas *produced by* pipelines, as well as gas purchased by the pipeline *from* its affiliate. The Conference Committee achieved that same result by a different mechanism: by including Section 601(b)(1)(E) in the NGPA, rather than by amending the Natural Gas Act. The proof that such section of the NGPA was intended to achieve the results that Sections 205

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[16] S.2104, as passed by the Senate on October 4, 1977. The text of Sections 205 and 206 are set forth in the Appendix to this brief.

and 206 of the Senate Bill, quoted above, would have also achieved—inclusion of pipeline produced gas in the comparable price limitation—is shown not only in the language of Section 601(b)(1)(E), but also by the June 6, 1978 working papers of the Conference Committee, the first three pages of which papers are set forth in the Appendix to this brief.[17] Appendix page 4a of such papers compares the provisions of the House and Senate bills under conference, which related to "Pass Through of Price Increases" by interstate pipelines. It is stated that Sections 205 and 206 of the Senate Bill guarantee pass through, "in the case of *sales between affiliated entities*", if the cost is not in excess of "the price received in comparable transactions by persons not affiliated with the pipeline." That language shows that the Committee and its Staff believed that the language "sales between affiliated entities" in their working papers, was the equivalent of the term, pipeline "purchases new gas from an affiliate *or produces new natural gas from its own properties*" in Sections 205 and 206 of the Senate Bill. "Sales between affiliates" was intended to include both sales by an affiliate to a pipeline, *and gas produced by the pipeline itself. And that "sales between" formulation is the one which was finally included in the NGPA, Section 601(b)(1)(E), which covers, it will be recalled, "the case of any first sale between any interstate pipeline and any affiliate of such pipeline"*. Whatever one may think of the drafting skill of the conferees, the intention is clear that the amount which could be put into a pipeline's cost of service, and thus recovered in its rates, for both gas which it produces itself and gas which it purchases from an affiliate, is limited by the comparable sales price limitation of the "affiliated entities limitation". That is what the Congress intended to do, and did, which shows that pipeline produced gas is the subject of a "first sale", that pipelines are not left free to price "gouge", and that

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[17] Those are the here relevant pages, but the full text of the working papers have been delivered to the Clerk of this Court, with this brief.

consumers are not left unprotected, by the "first sale" definition adopted by the Court below.[18]

In contrast, the FERC statutory interpretation would include only a *very* small amount of pipeline produced gas in the "first sale" category, and exclude the great bulk. But Section 601, and its legislative history, like Section 2(21), does not divide pipeline produced gas into categories, or say that some of it is subject to the section, and some not: it provides and assumes that *all* pipeline produced gas, like all other gas, is the subject of one "first sale," and is subject to the affiliated entities limitation.[19] The FERC interpretation, in contrast, would produce the discriminatory result that *no* pipeline produced gas, but *all* affiliate produced gas, is subject to the statutory affiliated entities limitation. That is not a credible result: it is inconsistent with the pattern, language and

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[18] It is not, of course, necessary for this Court to make a *holding* as to the scope of Section 601(b)(1)(E), since that is not the issue in these proceedings, but that Section does support the plain meaning of the dispositive Section 2(21) of the NGPA.

[19] Petitioners point to the lack of a contract between the pipeline's producing and transmission divisions and claim that Congress could not have intended to allow NGPA prices, rather than FERC jurisdiction, to be the limit on the values assigned to pipeline produced gas in the pipeline cost of service, since pipelines would not have the "contract limitation" on such values which independent producers have. However, the applicability of the affiliated entities limitation to pipeline produced gas, *inter alia*, shows that this point is illusory: that limitation is, for pipeline produced gas and gas produced by pipeline affiliates, the substitute for "arms length contracts." The FERC, of course, with oversight from the pipeline's customers and interested state agencies and consumer groups, polices that limitation. These considerations also show that claims relative to the inapplicability of Section 315 of the NGPA, 15 U.S.C. § 3375, to pipeline produced gas are frivolous: that Section provides potential rights to pipelines which are irrelevant when the pipeline is itself the producer, and possible information to the FERC from other producers which it can derive from *pipelines* under its Natural Gas Act authority.

legislative history of the NGPA.[20] The interpretation of Section 601(b)(1)(E) set forth herein, on the other hand, provides full consumer protection and is consistent with the sensible interpretation of "first sale".

B. The Legislative History And Purposes Of The NGPA Strongly Support The Decision Below

Petitioners admit that there is no legislative history which in any way contradicts the clear meaning of Sections 2(21) and 601(b)(1)(E) of the Act, described above. That statutory language is therefore determinative of the case, since if there is no clearly expressed legislative intention to the contrary, the language of a statute governs and judicial inquiry is concluded.[21] Here, there is not even any hint in the legislative history—or, as shown above, the statutory language—that the Congress intended, as the FERC claims, to carve out an ex-

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[20] Petitioners also attempt to deflect the inference raised by Section 203(b) of the NGPA, 15 U.S.C. 3343(b), that the use of the term "first sale acquisition costs" there, in relation to "any natural gas produced by any interstate pipeline or any affiliate of such pipeline", shows that Congress contemplated that pipeline produced gas and affiliate produced gas, like all other gas, would be the subject of a first sale. Petitioners argue that if Congress believed such gas would be the subject of a first sale, it need not have directed the FERC to determine the "first sale acquisition cost" for pipeline produced gas, but could have assumed that the "price paid" would be used, pursuant to Subsection (1) of the Section. But that is obviously not correct, since Congress knew that there is no "price paid" when a pipeline acquires gas which it produces itself, so the Subsection (1) wording does not fit. And Congress also clearly wanted to do here, what it did in Section 601(b)(1)(E): provide a special rule for gas produced by affiliates of pipelines, and pipelines themselves, to substitute for arms length bargaining (here in relation to the "incremental pricing" which is the subject of Section 203) for consumer protection relative to total pipeline rates, while applying NGPA price ceilings to the produced gas itself. And again, no distinction is created between pipeline produced gas and affiliate produced gas, or between categories of pipeline produced gas.

[21] Rubin v. U.S., 449 U.S. 424, 430 (1981); Consumer Product Safety Commission v. GTE, 447 U.S. 102, 108 (1980).

ception to exclude almost all pipeline produced gas from the generally applicable NGPA pricing system, much less the required "clearly expressed legislative intention" to create such exception.

Petitioners, however, try to reverse the principles of statutory construction, by claiming that if the NGPA is to be interpreted as replacing the FERC's "forty years" of past authority to itself impose price controls on pipeline produced gas, there must be legislative history showing a specific intent to do so. But that position conveniently and completely overlooks the fact that the entire NGPA—relative to all gas, not just pipeline produced gas—is devoted to reversing FERC practices, policies and results, as described earlier. Drastic changes to decades of FERC practice is exactly what the Congress intended to accomplish, and did accomplish, in enacting the NGPA, including imposing Congressional price ceilings on *intrastate* gas, and having *Congress, not the FERC*, set all gas price controls. Imposing Congressional price ceilings on intrastate gas, and taking control of all independent producer pricing from the FERC, were much larger changes than taking control of pipeline production pricing from the FERC. Thus, it is not surprising that—as the Court of Appeals found—the NGPA substituted Congressionally fixed price ceilings in place of FERC prices relative to pipeline produced gas, just as it did as to *all other* gas. And why should legislative history address a desire to affect only pipeline produced gas, when it addresses the fact that *all* gas is to be drastically affected by the NGPA, which obviously *includes* pipeline produced gas?

That is exactly what the legislative history of the NGPA shows, as demonstrated below, and that fact gives additional, albeit not required, support to the Decision below. The NGPA was enacted to secure for the nation an adequate supply of natural gas, by elimination of pricing disparities created by different regulatory methods in the in-

terstate and intrastate markets, and by Congressional mandate of the incentives of higher prices for gas producers.[22] Even the FERC admits that.[23] But the FERC holding produces different pricing depending upon the corporate form of the producer, which is not consistent with the NGPA policy of establishment of a single, comprehensive pricing policy: the FERC admits that companies affiliated with pipeline companies, even including companies *owned by* pipelines, *must be* allowed to use NGPA prices, but denies that for gas produced by the pipelines themselves. Thus, the FERC position is that Congress created a substantive distinction, based solely upon corporate *form*, but all without so stating in the statute or legislative history. Such claims of surreptitious discrimination are not supportable. The FERC interpretation also violates that uniform pricing pattern of the NGPA by requiring differing standards as between pipeline and distributor produced gas, depending upon whether the company is regulated by the FERC or a state agency. The FERC order also discourages pipeline production, and therefore is inconsistent with the policy of increasing domestic natural gas supply. (See Section III, below) This is particularly undesirable, since pipeline production is certain to be used to supply pipeline customers and make pipelines less dependent on other producers of gas, and thus better able to bargain for economical purchases of the remaining gas they require. Therefore, pipelines should be regarded as desirable producers of gas, as the FERC, in

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[22] The comprehensive NGPA pricing provisions provide higher prices for producers of natural gas, and immediate or ultimate decontrol of prices of some categories of gas. The higher revenues provide not only capital necessary to achieve increased production from gas reserves, but also increased incentives to do so. Congress felt that higher prices which elicited greater domestic gas supplies would be a more economical energy initiative than use of imported energy, or higher cost domestic alternative energy sources.

[23] See, for example, Petition for Writ of Certiorari of FERC at 7-9, and App. B-51.

other proceedings, has held.[24] Yet, the FERC Orders here under review would discourage such production.

The intention of Congress to create a *uniform* national gas producer pricing policy, applicable to *all* gas and not controlled by or based upon the FERC cost method of regulation, is *clear* from the legislative history of the NGPA. The intention to cover *all* gas, whether interstate or intrastate, is shown by the Senate Energy Committee's summary of legislative activities in the 95th Congress, which states that the NGPA "specifies ceiling price levels *for all natural gas production*, which increases with inflation";[25] the House reference to the NGPA establishment of "a statutory price control formula applicable to both interstate and intrastate sales";[26] by Conference Report reference to NGPA applicability to "any" natural

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[24] That FERC policy was expressed in such orders as "Pipeline Production Area Rate Proceeding (Phase I)," Docket No. RP66-24, 42 F.P.C. 738, 752 (1969), *reh. denied*, 42 F.P.C. 1089 (1969), where the FERC said that "pipeline producers are henceforth to be treated on a parity with independent producers. By so doing, we are encouraging intensified exploration by the pipeline producers." In Opinion No. 47, *Columbia Gulf Transmission Co., et al.*, Docket No. RP75-105, *et al.*, July 2, 1979, the FERC refused to adopt rate treatment under which the pipeline system's rate of return *"would be lower than those of independent producers and therefore its ability to compete for leases and develop marginally profitable reserves would be impaired."* (Opn. at 12, n. 19, emphasis added). The Commission went on to say that (Opn. at 13, emphasis added, footnotes omitted): "The Department of Energy Organization Act of 1977 and the Natural Gas Policy Act of 1978 express legislative judgments that the Nation's energy needs are more acute than ever. The latter statute is very much to the point here. *The Congress obviously attached greater weight to inducing companies to go out to look for gas than it did to the previous consumer-protection objective of narrowly-defined cost-based rates for discovering and producing gas supplies.*"

[25] S. Rep. No. 43, 96th Cong., 1st Sess. 6 (1979) (emphasis added).

[26] Staff of Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 2d Sess., "Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978" (Comm. Print. 62) at 1-2.

gas;[27] by references of House Chairman Dingell to the "single national market" created by the NGPA[28] and to the Act's broad applicability;[29] and by earlier Senate reference to the need to abolish "the artificial distinction between the interstate and intrastate markets".[30] Yet, the FERC Orders here under review would make the NGPA inapplicable to almost all pipeline and distributor produced gas. As the Court of Appeals held:

> With respect to the goal of eliminating a dual market structure, the Commission's order would exclude virtually all interstate pipeline, intrastate pipeline and local distribution company production from the NGPA's uniform prices. While the Commission would retain control of interstate pipeline production under the NGA, the effect of its order would be to leave intact state regulation of intrastate pipeline and local distribution company production. The intrastate market for such production would thus be perpetuated. This would leave a substantial vestige of the dual market structure Congress sought to eliminate. 664 F.2d at 536.

The Court is quite correct. The FERC would have NGPA maximum prices limit independent or affiliated producer prices for gas sold in both intrastate and interstate commerce, but there would be no NGPA limit on prices intrastate pipelines and distributors could charge for gas which they produce and sell in intrastate commerce: that would be subject to state discretion totally. Meanwhile, the FERC would control almost all interstate pipeline production, at *its* discretion. It will be recalled that it was while the states totally controlled

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[27] H.R. Conf. Rep. No. 1752, 95th Cong., 2d Sess. 74 (1978), *reprinted in* 1978 *U.S. Code Cong. & Ad. News*, 8983, 8991.

[28] See statement of Rep. John Dingell, Chairman of the House Committee on Interstate and Foreign Commerce, 124 *Cong. Rec.* H13114 (daily ed. Oct. 14, 1978).

[29] 124 *Cong. Rec.* H13118 (Oct. 14, 1978).

[30] S. Rep. No. 436, 95th Cong., 1st Sess. 21 (1977).

intrastate gas and the FERC controlled interstate gas that the inequities and disincentives were produced which led to a glut in the intrastate market and gas shortages in the interstate market. The NGPA was passed to remedy, not perpetuate, such conditions.[31]

The legislative history also shows the intent of Congress to abandon the FERC's "cost based" method of producer price regulation,[32] but, the Commission Orders here under review would continue that method for almost all pipeline produced gas.

Finally, the NGPA has no language, and no legislative history, indicating any intent to exclude some producers of gas—pipeline producers or others—from the NGPA. Instead, the House Energy Subcommittee's Counsel simply noted, relative to a forerunner bill, "the definition of the term producer, meaning a person who produces gas",[33] without carving out any exception for pipelines which produce gas, as the FERC now tries to do. And in that same hearing on bills which led to the NGPA, a former FERC official testified that "[t]here is no doubt that the major interstate pipelines (as well as distributors with producing affiliates) will benefit from the pricing provisions because all of them have producing affiliates or *divisions.*" (emphasis added).[34] That statement

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[31] The FERC brief's suggestion (pp. 29-30) that the above problems assume "intrastate pipelines would somehow extend their operations into the interstate markets" is inaccurate and incomprehensible: no such assumption is involved or needed.

[32] See n.26 and Statement of Rep. John Dingell, Chairman of the House Interstate and Foreign Commerce Committee, 124 *Cong. Rec.* H13114 (daily ed. Oct. 14, 1978).

[33] Hearings on H.R. 6831, *et al.*, before the Subcommittee on Energy and Power of the House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess., ser 23, Pt. 2 (1977), 913-973, 968. As noted earlier, the definition of "first sale" which was written does not distinguish between pipeline and other production.

[34] Hearings on H.R. 6831, *et al.*, before the Subcommittee on Energy and Power of the House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess., ser 23, Pt. 2 (1977) at 894.

—that gas produced by a pipeline's producing *division*, as well as its affiliate, would receive NGPA prices—was not disputed by anyone, and thus is a relevant and useful fact of legislative history.[35] *Arizona* v. *California*, 373 U.S. 546 (1963). The "unless clause", discussed in Section I A 1 of this brief, was included in Section 2(21) of the NGPA to insure such applicability of the NGPA, and that result is emphasized by Sections 601 and 203, which assume and indicate that pipeline produced gas is the subject of "first sales".

II. THE COURT BELOW PROPERLY REJECTED THE CLAIMS OF PETITIONERS

The Decision below leaves intact the FERC authority to regulate pipeline resale and transportation rates under the Natural Gas Act. Thus, the FERC admits (Brief at n.24) that the issue here is *not* whether pipeline rates will be unregulated. Instead, the issue is whether Congress, or the FERC instead, has the authority to fix the pricing system which controls the gas cost component of the overall pipeline rates which the FERC will authorize. Everyone, including the FERC and other Petitioners here, agrees that as to the great bulk of the produced gas, the Congress eliminated the FERC power and responsibility, and has substituted Congressionally fixed, NGPA prices. But Petitioners assert that a narrow exception was created by the NGPA, but *sub silentio*. The errors of that assertion are shown below.

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[35] Curiously, certain Petitioners claim that the fact that bills enacted in the 1950's, one of which would have deregulated pipeline produced gas and one of which would not, somehow show that the NGPA was intended not to include pipeline production. In fact, however, such bills and the above testimony of the FERC official show that Congress has uniformly dealt with pipeline production directly. In the NGPA, that was done in the "unless clause" of the definition of "first sale", in Section 2(21), because the NGPA makes the "first sale" the operative factor for applicability. In earlier bills, with no use of the "first sale" concept, the *language* used to deal with pipeline production was different, but similarly dispositive.

A. The Interpretation Of The NGPA By The FERC Is Erroneous, Illogical And Discriminatory

The FERC seeks to retain control over a share of gas producer pricing, but faced with the language of Section 2(21) of the NGPA, the FERC cannot contend that *no* pipeline produced gas is the subject of a "first sale." So the FERC has instead selected an interpretation of that phrase which the FERC and everyone else agrees would exclude from the "first sale" definition, *almost all* gas produced by pipelines. (App. B-3, B-19) But at the same time, the FERC admits (App. B-9, 10; B-12, 13) that *no* gas produced by pipeline affiliates is excluded from that definition. Yet, pipelines and affiliates are referred to in exactly the same way in the controlling language of Section 2(21) of the NGPA: it can be seen that there is no differentiation in the statutory language which could justify the totally different treatment which the FERC interpretation requires. There is also no reason, or indication, why the Congress would have wished to discourage pipeline production, and encourage putting that production into an affiliate. There is also no indication that Congress wished to reward companies which developed their production in, or spun it off to, affiliates, before the NGPA, and penalize those which have continued to produce gas themselves. There is no support for the claim that Congress desired any of such discriminatory and irrational results, and the Court of Appeals rejected the FERC interpretation which would produce such results.

The FERC tries to exclude almost all pipeline produced gas from the "first sale" category by claiming that only if gas produced by a pipeline is sold to a buyer before that gas is "commingled" with any other gas, may that gas be the subject of a "first sale".[36] But that seldom happens. Typically, gas produced by a pipeline is, shortly after it

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[36] If the concept is adopted that the first sale occurs at the transfer from pipeline producing properties to pipeline transportation facilities, then this alleged "requirement" is met. (See Section II C, below)

leaves the well, mixed with other gas in one or a series of "gathering" and/or transmission pipelines. In those situations, which involve almost all pipeline produced gas, the FERC admits it would deny "first sale" status. Thus, the FERC would make the "first sale" definition depend upon whether the gas produced by the pipeline is "commingled", and when. But the statute does not even mention commingling. The Section 2(21) definition does not refer to the concept or use the term or suggest, in any other way, that some gas produced by pipelines is to be accorded NGPA "first sale" pricing status, and some is not: there is no differentiation between "types" or "categories" of gas at all. There is no suggestion that any gas produced by pipelines or their affiliates is to be denied "first sale" status. As to pipeline affiliate production, the FERC honors that fact. But as to pipeline production, it does not. The distinction is without lawful support, and constitutes invalid discrimination, as discussed below.

The FERC and other Petitioners reach their invalid conclusion by an insupportable interpretation of the term "attributable". Under Section 2(21), a sale is a "first sale" if "such sale is attributable to volumes of natural gas produced by" the pipeline. The obvious reading of that quoted phrase is that any gas sold which has been produced by the seller (so that such volumes are "attributable" to produced gas) is the subject of a "first sale". That leaves the gas purchased and resold by such seller as non-"first sale" gas, since such gas will have already been the subject of a "first sale" when sold by the producer of that gas. The FERC, however, claims that the words "attributable to" means that the FERC has been granted discretion to decide which sales are to be considered "attributable to" gas produced by a pipeline, irrespective of the actual production. That claim appears in the "Attribution Rule" [37] which creates the commingling concept: the

[37] Section 270.203(a), promulgated by Order No. 58. The name of the "attribution" rule is an effort to fit in with the term "attributable" in Section 2(21) of the NGPA, but such obvious manipulation of terms does not constitute statutory interpretation.

claim that if the pipeline produced gas is "commingled" with other gas before it is sold, there is *never* a "first sale" of the pipeline produced gas, even though that would be the *only* gas in the nation which would *never* be sold in a "first sale." Thus, the FERC interprets the term "attributable" to mean "comprised exclusively of gas from identifiable wells, properties or reservoirs." That is clearly not a normal reading of the word attributable, nor is there support for such meaning in the NGPA or its legislative history.[38] Further, the statutory pattern which would have been created, if the Court of Appeals had allowed that strained construction to stand, is irrational.

1. The "unless clause" is construed by the FERC as having been inserted into the NGPA to cover almost no gas, and the NGPA is construed by the FERC to impose uniform Congressional price ceilings on all gas produced by persons not affiliated with pipelines, *and* all persons affiliated with (owned by, or owning, or having common ownership with) pipelines, *but not* by pipelines themselves. The NGPA also is construed by the FERC as giving the FERC the power to pick and choose *which* pipeline produced gas will be awarded NGPA prices, in further violation of the uniform Congressional price limits of the NGPA. Such pattern is not credible.[39]

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[38] The FERC Brief, p. 17, cites two other places where the word "attributable" is used in the NGPA, and says it was "used to limit the applicability of certain provisions." Of course it was, just as it is used in Section 2(21) to limit the "unless clause" to gas produced by pipelines. But nowhere is "attributable" used to mean "comprised exclusively of", as the FERC claims. Its own citations undermine that position.

[39] Such a discriminatory interpretation of the NGPA is invalid as creating arbitrary and discriminatory classifications of producers of natural gas, completely unrelated to the Congressional purpose expressed in the NGPA of increasing production of natural gas and of replacing the previous cost-based methodology of pricing such gas with a comprehensive, legislatively established pricing scheme. United States Dept. of Agric. v. Moreno, 413 U.S. 528 (1973). Such FERC interpretation would make the NGPA invalid

[Footnote continued on page 28]

2. The FERC's interpretation disadvantages and discourages pipeline production, and gives incentive to switch production to affiliates. It is not credible that Congress desired such result.[40]

3. The FERC's attempt to describe what pipeline produced gas would be covered by "first sales" shows the irrational nature of the interpretation which was rejected by the Court of Appeals. The FERC first says that if the sale is made by the pipeline "at the wellhead, in an offsystem sale", it would be a "first sale". (App. B-2) In other words, if a pipeline sells its gas "offsystem" (meaning, to purchasers other than its on system customers who depend upon it for gas supply), then it cannot be denied the stimulus of NGPA prices, but if it uses the gas to meet part of its on system customers' requirements, it does not receive such incentive. How that fits with the policy of the NGPA, to increase gas supply to

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because it would discriminate against pipeline production on the one hand, as compared to independent producer production and affiliate production on the other, in violation of the Due Process and Equal Protection Clauses of the Constitution. It would mean that persons are not being treated alike under similar circumstances and conditions, and thus have unequal liabilities imposed upon them. Schneider v. Rusk, 377 U.S. 163, 168 (1964); Currin v. Wallace, 306 U.S. 1 (1939); Reagan v. Farmers Loan and Trust Company, 154 U.S. 362 (1893). Such discriminatory result would also mean that Section 270.203 of the Commission's Regulations is (1) "contrary to constitutional right, power (and) privilege" and (2) "in excess of statutory jurisdiction, authority, or limitations or short of statutory right," in violation of Sections 706(2)(A), 706(2)(B), and 706(2)(C) of the Administrative Procedure Act, 5 U.S.C. § 500, *et seq.*, as well as the NGPA. Such an interpretation is to be avoided if feasible, to save the validity of the statute.

[40] The FERC's uneven interpretation also drives the FERC to the creation of an incredibly self-contradictory "circumvention rule", which first contradicts its "attribution rule" to make sales of "commingled gas" (which includes pipeline produced gas) "first sales", but then inserts an exception which eliminates almost all such sales from the rule. (See Section 270.203(b) of FERC regulations, App. B-12). There will be no need for such Section at all if the uniform applicability of the "first sale" definition prescribed by the Court of Appeals is allowed to stand.

the customers dependent upon pipeline supply, the FERC and other Petitioners do not—and cannot—explain. There is no indication Congress desires such result, and every reason why it should not desire it.[41]

4. The FERC also says that a pipeline could "dedicate natural gas which it produced from an identifiable source to a particular purchaser by contract, commingle the gas with general system supply gas and withdraw equivalent volume for delivery to that purchaser" and "the sale would generally qualify as a first sale" because "the source of the gas is identified and the FERC could be assured the gas is 'attributable' to the pipeline's own production". (App. B-3). In other words, if pipelines changed their present pattern, of treating gas which they produce as part of their general gas supply, and instead artificially divided the gas supply *contractually* (not physically), they could receive NGPA prices: that is, the gas from each of the pipeline's producing wells or fields would be contractually assigned to a particular customer in separate contracts (presumably with enough *purchased* gas also separately being contracted to such customer to make up the total volumes the customer needs). Thus, a complicated change of *contracting form* only would cause a different economic result: that makes no legal or economic sense and is not permitted by, or consistent with, much less required by, the NGPA.

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[41] Petitioners claim that the small volumes of gas sold in such offsystem sales have received "independent producer treatment" (area and national rates), apparently in an effort to make that category sound meaningful enough to justify having the "unless clause" devoted only to it. In fact, however, production by pipelines from post 1969 leases also has received "independent producer treatment." Therefore, if Congress had wanted to exclude gas which received cost of service treatment from NGPA pricing, it would have said so. But Petitioners are instead forced to make the inconsistent claim that the NGPA provides that offsystem sales which formerly had "independent producer treatment" are the subject of "first sales", but gas sold from new leases, which also had "independent producer treatment", is not. Petitioners' problem is that the facts do not fit the theories they have devised to try to reach their desired result.

5. The FERC's interpretation leads to totally irrational results. Gas produced from a well by a pipeline, and sold by itself to a buyer, would be covered as "first sales", but gas produced from the same well by the same pipeline and sold to the same buyer at the same point, would not be covered if it had been "commingled" with other gas before delivery to the buyer. That would be FERC created economic nonsense of the type the NGPA was enacted to stop, not create. Another example of the lack of logic of the FERC claims is that when, as is often the case, an independent producer and a pipeline share ownership of the same well, the former could receive NGPA prices for its share of the gas, but the pipeline could not. Further, even though the FERC claims that former cost of service treatment should prevent "first sale" treatment, pipeline produced gas, *whether or not previously regulated on a cost of service basis*, is given "first sale", NGPA pricing treatment if sold "uncommingled": but gas sold commingled can never be the subject of a "first sale," according to the FERC, even if never regulated on a cost of service basis. What all this shows is that the Commission is unable to come up with even a distorted interpretation of the NGPA which fits its ostensible rationale for denying NGPA pricing to some gas. Further, the policies it is trying to impose do not carry out that rationale consistently.[42]

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[42] Further examples of the FERC Orders here under review demonstrating that the FERC is not applying its own rationale consistently include (App. B-9) the FERC assertion that its regulations (App. B-12, 13) classify sales by affiliates as "first sales" by use of FERC authority under Section 2(21)(A)(v) of the NGPA to include sales as "first sales". But that is neither accurate nor necessary, because under the FERC interpretation of the basic rule of Section 2(21)(B) (as well as under Respondent's different interpretation), such sales *are* first sales by nature (because, to use the FERC rationale, they are made exclusively with gas produced by the affiliate, and thus qualify). Therefore, there is no need to use Section 2(21)(A)(v), but the FERC is confused on this point because it assumes erroneously that it is almost totally free to pick and choose as to which pipeline or affiliate produced gas sales are "first sales."

6. The FERC and other Petitioners also claim that use of the term "Wellhead Pricing" in the heading of Title I, Subtitle A of the NGPA, and a reference to "field sale" by a Congressman, somehow evidences a Congressional intent to exclude pipeline produced gas from the "first sale" definition, because sales by pipelines to their customers are normally at the wellhead or in the producing field. But the FERC's own Order No. 58 admits that all sales by *non-pipeline producers* are "first sales", whether made at the wellhead, *or far from the wellhead* at the end of extensive gathering (or even transmission) lines, or at the outlet of gas processing plants located far away from the wells. Further, Order No. 58 would classify sales of *pipeline produced* gas as "first sales", *even if made far from the wellhead*, so long as the gas is not physically "commingled", *or* is contractually separated, as discussed above. The Court of Appeals correctly noted this point, stating that the "Commission's Order No. 58 is inconsistent with this reasoning" (the claim that the use of the terms "wellhead" or "field" sales means that sales of pipeline produced gas cannot be first sales) because that same Order "recognizes that non-wellhead sales may be first sales. Order No. 58 would allow as a first sale a downline sale to a pipeline customer if the sale was exclusively attributable to pipeline production despite the fact that such a sale is no more a wellhead sale than is any other pipeline customer sale." 664 F.2d at 536. In addition, the "wellhead pricing" argument has also been destroyed by Petitioners' admissions, in their briefs to the Court of Appeals, that "some non-wellhead sales can be 'first sales'." (FERC Br. 19, 22; New York PSC Br. 2, 7, 10.) Since it is conceded that the use of the heading "Wellhead Pricing" in Title I, and references to field sales, do not limit *all* "first sales" to sales at the wellhead, that heading thus gives no indication at all that *any* non-wellhead sales by pipelines are not "first sales."

Given the above described unsupported and irrational aspects and results of the FERC's interpretation of Section 2(21) of the NGPA, refusal to defer to any alleged ex-

pertise of the FERC is wholly justified. Courts are the final and expert authorities on issues of statutory construction and interpretation, not the FERC.[43] Administrative interpretations must be reversed when inconsistent with statutory language or intent, or with legislative history, and an agency may not restrict or enlarge the statute.[44] The Court of Appeals (644 F.2d at 534-536) also noted that the factors militating in favor of deference are missing here: the FERC interpretation has not withstood a long period of use without challenge from Congress and does not involve terms or matters relative to which the FERC has expertise (since the term "first sale" is new to the FERC and there is no indication that the FERC had any input into the definition).

Petitioners allege that the "contemporaneous interpretation" by the FERC deserves deference. But they conveniently neglect to mention that the first FERC interpretation of the Section 2(21) "first sale" definition, which *was* relatively contemporaneous, was *inconsistent* with the different definition adopted later in Order No. 58, which is here under review. That is, the FERC's first interpretation of Section 2(21), less than one month after the statute was enacted, claimed that sales of gas by *both affiliates of pipelines*, and by pipelines, are not first sales. (Interim Rules, Docket No. RM79-3, 43 F.R. 56448

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[43] SEC v. Sloan, 436 U.S. 103 (1978); NLRB v. Brown, 380 U.S. 278 (1965); FTC v. Colgate-Palmolive Co., 380 U.S. 374 (1965). Consistently, Section 501 of the NGPA gives the FERC authority to define only "accounting, technical and trade terms", and then only "consistent with the definitions set forth in this Act."

[44] *See* Int. Bhd. of Teamsters, etc. v. Daniel, 439 U.S. 551, 568 n. 20 (1979); Mohasco Corp. v. Silver, 447 U.S. 807 (1980); Shea v. Vialpando, 416 U.S. 251 (1974); Morton v. Ruiz, 415 U.S. 199 (1974); Espinoza v. Farah Mfg. Co., 414 U.S. 86 (1973); Fed. Mar. Comm. v. Seatrain Lines, Inc., 411 U.S. 726, 745 (1973); Volkswagenwerk Aktiege. v. Fed. Mar. Comm., 390 U.S. 261, 272 (1968); NLRB v. Brown, 380 U.S. 278, 291 (1965); Davies Warehouse Co. v. Bowles, 321 U.S. 144 (1944); Neuberger v. Comm'r, 311 U.S. 83 (1940).

(Dec. 1, 1978)). But the FERC reversed itself in November, 1979, in Order No. 58, and ruled that affiliate production does qualify for "first sale" treatment, but still claims that most pipeline production does not. It is obvious that it is not expertise that is at play, but rather an inconsistent FERC effort, irrespective of Congressional intent, to maintain the authority which Congress has taken from it. The principle which is most applicable is that reversal is needed where an "agency's interpretation departs so widely from the statutory mandate that it is explicable more easily as an organic reflex to *extend its own jurisdiction than as a reasoned interpretation of the statute.*" *Usery* v. *First National Bank of Arizona*, 586 F.2d 107, 111 (9th Cir. 1978) (emphasis added).

In short, the Court of Appeals was clearly correct when it held: "In sum, these factors fall far short of demanding a deference to the Commission's interpretation of the statute which could challenge the clear meaning of a statute as revealed by its language, purpose and history." 664 F.2d at 535.

It is apparent that the FERC, in Order No. 58, has attempted to seize "discretion" to allow it to try to retain control over the bulk of pipeline produced gas, even though Congress provided to the contrary. And the fact that in Order 98, the FERC has exercised its purported discretion to "allow" NGPA pricing to the larger share of pipeline produced gas does nothing to correct the FERC's error in statutory interpretation. As a matter of law, that interpretation is in error, and as a practical matter, if the FERC is allowed to seize the purported discretion which it claims to exist, it could later choose to use that discretion to discriminate against even that larger share of pipeline produced gas as to which, in Order No. 98, it allowed NGPA pricing. It is exactly that discretion, and the uncertainties and lack of incentives which were created thereby, which Congress chose to take away from the FERC, when it enacted the NGPA. In contrast, the Court of Appeals' interpretation gives

equal treatment to all pipeline produced gas, and also gives equal treatment as between gas produced by pipelines, by affiliated producers and by other producers. Petitioners complain that such parity of treatment is inconsistent with the pipeline production practices of the FERC, prior to the NGPA. But they ignore the fact that changing FERC practices is exactly what the NGPA did do, and was intended to do, relative to *all* gas produced: it would be anomalous if the Act were interpreted to *not* do so, as to *only* pipeline produced gas.

B. The Decision Below Does Not Impede The Regulatory Duties Of The FERC Or The States

The FERC claims that having all gas produced by pipelines and distributors be subject to the NGPA pricing provisions will somehow obstruct gas price regulation. In fact, as demonstrated, the NGPA takes control of the price allowed for the *gas* itself away from the FERC, and substitutes the Congressionally fixed gas pricing provisions. At the same time, there is no interference with the FERC regulation of the rates which interstate pipelines may charge, or of state agency regulation of the rates of instrastate pipelines and distributors: neither the FERC nor state regulatory agencies have been ousted from their authority and duty to regulate gas *resale* rates, by either the NGPA or the Decision below. The regulation of such rates charged by interstate pipelines will continue by the FERC, as will regulation of intrastate pipeline and distributor rates by the applicable state body, just as before the NGPA. The methodology used will continue to be the "cost of service" basis, under which the regulatory agency will determine all of the various allowable costs of the pipeline or distributor, for the receipt, transportation, storage and sale of the gas. Such costs include all operation, maintenance, and administrative costs, depreciation, and cost of capital (computed as cost of plant in service—rate base—times rate of return—a function of capital structure and debt and equity costs). Those costs will continue to be determined by the FERC and state agencies. To those costs are added the cost of gas which is

purchased and resold by the pipeline or distributor (now conceded by all to be subject to NGPA limits), and also the appropriate amount for the gas which the pipeline or distributor produces itself from its own gas reserves, which it also sells to its customers. Before the NGPA, the FERC, for interstate pipeline produced gas, and state agencies, for intrastate pipeline and distributor produced gas, determined the ceiling amounts to be included in the cost of service for gas *produced* by pipeline producers *and other producers.*[45] Now, the NGPA fixes the price ceilings and that substitution of Congressional price limits for regulatory limits is the purpose of the NGPA.

But substitution of Congressional provisions changes only one step of the regulatory process. All that the FERC and state agencies must do is allow the company to substitute those Congressionally limited values for the gas itself, in place of the values which those agencies themselves previously determined, and carry on the same as before in all other ways. In fact, the FERC has itself shown that such process is workable, and will not impede its regulatory activities, by already voluntarily adopting (App. B-14) the same regulatory procedures, for most pipeline produced gas, which the Court of Appeals' Decision requires for all such gas. This is also the same process that the FERC has used for well over a decade: adding unit rates for the gas itself (then area or national rates, now NGPA rates) to other piplines costs, to derive the overall costs of service used to compute pipeline rates. It is obvious that since the FERC has, can, and desires to,

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[45] The FERC originally used, for *non*-pipeline producers, and pipeline producers, an individual company cost of service basis. But later the FERC came to apply the cost based area or national group rate method to independent producers, and also then applied that methodology to new pipeline and pipeline affiliate production, in substitution for a determination of actual costs of production of the individual pipeline, to calculate the total "cost of service" used to determine overall pipeline rates.

regulate a *portion* of pipeline produced gas in exactly the way that the Court of Appeals has held is required, it clearly *can* implement the pricing provisions of the NGPA for *all* such gas in the same way. In fact, maintaining two separate methods of regulation, as the FERC desires to do, is far more cumbersome than maintaining only one, by simply implementing the pricing provisions of the NGPA, as the Court of Appeals directs.[46] Further, the Decision below requires use of the *less* cumbersome method, since it does not require a separate determination of a utility-type cost of service for pipeline production, but simply allows the rates set by Congress.

The FERC claim that the Decision below interferes with the regulatory authority of the states is equally inaccurate. State agencies will continue to follow the same cost of service computations as have been described above, in fixing rates for intrastate pipelines and distributors. The state agency will continue to determine all allowable costs of the intrastate pipeline or distributor, including the "gas component" costs, now subject only to Congressional ceiling prices as to the gas component.[47] That

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[46] The most clear showing that the claim of regulatory difficulty is false is the situation of Michigan Wisconsin, where the FERC approved a rate case settlement under which the method of pricing the gas produced by the pipeline will be the same one which is *required* under the Court of Appeals' Decision. Thus, there will be absolutely no difference in "administrative burden" if the Court of Appeals' Decision is affirmed: the FERC will continue to use the same method it has already voluntarily adopted. (In fact, the FERC, in 1977, *required* Michigan Wisconsin to utilize the unit rate method which the FERC now claims is burdensome.) The above settlement also means that, for Michigan Wisconsin, the issue in this case is whether it will be allowed to recover the sums it was forced to pay (improperly, it is submitted), in order to achieve NGPA pricing, like other producers. For other Respondents in this case, the issue is whether they will be allowed to achieve that equitable pricing parity.

[47] Section 602(a) of the NGPA, 15 U.S.C. § 3432(a), ("Effect on State Laws"), provides that states may "establish or enforce any

[Footnote continued on page 37]

change was intentionally created by the NGPA, because the price of gas itself is exactly what Congress did limit, as to the states, just as it removed such control from the FERC, by enactment of the NGPA. But the state agency, like the FERC, will still set the components of the rates charged by companies they regulate, while use of Federal price limits for the cost of the gas itself will not cause any burden to the state agency or the FERC. They will simply apply prices no higher than the Congressionally set prices to the gas volumes, and add the resulting cost to the other cost elements of the company, which the agency will determine, in order to determine the utility cost of service. The only "interference" with retail rates is that imposed by the NGPA, the new requirement of NGPA (Congressional) pricing limits, for *all* gas produced and sold in the United States.

But since everyone agrees that Congressionally set rates apply to the bulk of the gas sold by intrastate pipelines and distributors (gas which they *purchase*), and the FERC and other Petitioners also agree that such Congressionally set rates apply to all gas produced by independent and affiliate producers, and to gas produced by instrastate pipelines and distributors which is sold before it is "commingled", obviously it will not burden a state if the same Congressionally set NGPA prices are also applied as a limit on the value of the rest of the gas which those companies produce.[48] No gap of consumer protection is created. The change is only that for which the

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maximum lawful price for the first sale" of gas produced within the state, *so long as it does not exceed the prices set forth in Title I of the NGPA*.

[48] The Michigan brief, at 9-10, argues that under the Decision of the Court below, states could not use the cost of service method to determine what price they will allow for gas produced and sold in intrastate commerce. But that is clearly wrong, since Section 602(a) of the NGPA allows states to establish maximum lawful prices for such gas (so long as they do not exceed NGPA limits), and does not prescribe or prohibit any method for doing so.

Congress enacted the NGPA: the change of producer price limits from FERC and state control to Congressional control.[49]

C. The Decision Below Is Correct, Irrespective Of Which Concept Of When The "First Sale" Takes Place Is Accepted

The FERC and its supporters claim that the Court below erred by indicating that a "first sale" is made when the gas produced by a pipeline or distribution company is transferred from the producing facilities of the company to the transportation facilities of the company. This claim is part of the continuing effort to draw attention away from the basic issue here: did Congress intend to cover *all* pipeline produced gas with its new ceiling prices, just as it covered all other domestic gas? As shown above, various parts of the NGPA language and legislative history show that Congress did so intend. The focus of the "first sale" concept is not upon a "sale", but upon its use as a drafting mechanism for identifying the producer of gas, because it is the producer of the gas whose revenues—for the gas itself—are limited to the NGPA ceiling prices. Some producers realize those revenues after adding to those prices, allowable taxes, "Btu adjustments" and other charges for producer services. Other producers—pipeline (and distributor) producers—realize the revenues by using the values allowed by the NGPA as a part of their cost of service which is used to derive their overall rates. The important point is that the Congress has provided that the FERC cannot deny the *pipeline* producer the right to realize the same values, relative to gas produced, as all other producers.

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[49] Apparently desperate for arguments, the FERC and some Petitioners also make the claim that the Decision of the Court below would mean that NGPA "first sale jurisdiction" would be extended to gas which is consumed by the producer itself. In fact, of course, there is no such effect, because such producers consume and do not sell their gas. In any event, the point could have no practical effect, since such companies have no cost of service in which NGPA values would be included. The whole claim is illusory.

In this context, the *point of* "first sale" is not the central focus: the identification of the producer is. And Section 2(21) of the NGPA clearly includes pipeline producers, with confirmation from other sections and legislative history.

The Court of Appeals conceptualized the "first sale" as an event, as well as a means of identifying producers, in a very thorough analysis and rounding out of its review of the relevant parts of the statute. In doing so, the Court viewed the transfer of gas from pipeline production facilities to pipeline transmission facilities as a logical, sensible point to use to depict the act of the pipeline producer which is the operational step at which its producing activities, which earn it the gas component of its overall cost of service, are consummated. That is a very reasonable, practical view of the facts in the industry. In addition, however, if one decides it is even necessary, for purposes of this case, to view the "first sale" as an event in time or space, the alternative concept which the Court of Appeals could have adopted, to reach exactly the *same end result*, is that the "first sale" occurs when the pipeline or distributor sells the gas it produces (together with gas it purchases) to its customers.

The important point is that this is a theoretical discussion of legal concept, and under either concept of the place of "first sale," the practical result, and the regulatory processes used, will be the same: the same NGPA price limits will be applied to the gas produced, and the value for produced gas will be added to all the other pipeline or distributor costs, to produce the same cost of service, as described in Section II B, above. Therefore, the result will be the same rates to consumers, under either concept, so that it is, in economic terms, irrelevant which concept is used. And real economic effect, not legal form, is controlling. *NLRB* v. *Hearst Publications, Inc.*, 322 U.S. 111 (1944); *United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392 (1965).

Petitioners, however, attempt to use their discussion of "point of sale" to claim that there is *no* "first sale" of pipeline produced gas, even though that is inconsistent with the pattern and purpose of the NGPA, which result Sections 2(21) and 601(b)(1)(E) of the NGPA were obviously drafted to prevent. But Petitioners claim that there cannot be a "first sale" without a transfer of title. That, they allege, wins the case for them. But it does not, for quite obvious reasons. First, as noted, determining the *point* of the "first sale" has no practical significance: "first sale" is a statutory *price and rate* concept, designed to attach a Congressional price limit to each unit of gas as the limit on recompense to the producer for production of that gas. It is a way of defining the producer, so as to fix the values the producers can receive. Second, if one wants to conceptualize a *point* of "first sale," using the definition of "sale", the reasoning of the Court of Appeals is highly sensible, because the definition of "sale" in Section 2(20) of the NGPA is "any sale, exchange or transfer for value." Since the word "sale" in the definition means a transfer of title for money, and "exchange" means a transfer by barter, "transfer for value" clearly contemplates other kinds of transactions. There are compelling arguments that transfer of possession of the gas, from pipeline production facilities to pipeline transmission facilities, without transfer of title, is such "transfer for value".[50] Thus, the Court below has a strong basis for its statement that Congress contemplated the "intracorporate transfer" as the *point of* "first sale".

In addition, however, Congress knew that *all* gas to which it wished NGPA price limits to attach is sold somewhere, and thus attached its prices to the "*first* sales" concept, as described above. In doing so, Congress was clearly aware that gas produced by pipelines, as well as by independent and affiliate producers, is sold: the

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[50] See briefs herein of Respondents Mid-Louisiana, *et al.*, Section I.B. and Consolidated Gas Supply Corporation, Section III.

pipeline sells the gas to other pipelines, or distributors, or directly to consumers. Thus, there is a sale of pipeline produced gas, *with transfers of title*,[51] so that *if* such were a requirement for there to be a "first sale", the requirement is met.

The important point is that there *is* a sale, which is a "first sale", of pipeline produced gas, and *wherever* it is held that the relevant "sale" for "first sale" purposes takes place, assuming such holding is required here at all, the statutory requirement is met and the related regulatory consequences and procedures will be exactly the same. Thus, if the Court of Appeals had held, or if this Court were to hold, that each "first sale" of pipeline produced gas occurs when title passes to the pipeline's customers, rather than at the intercompany transfer point, the Decision of the Court of Appeals—that pipeline produced gas is the subject of a "first sale", and thus is controlled by NGPA, not FERC, pricing —should be affirmed on that basis, too.[52] There can be

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[51] This fact also makes irrelevant the claim of Petitioners that the FERC has authority to define intracorporate transfers as *not* "transfers for value" under a Conference Committee Report reference to FERC power to "define terms such as transfer for value" used in the definition of "first sale; it may also establish rules applicable to intracorporate transactions under the first sale definition." H.R. Rep. No. 1752, 95th Cong., 2d Sess. 116, *reprinted in* [1978] U.S. Code Cong. & Ad. News 8800, 9033. The Court below held that such reference "assumes that intracorporate transactions will fall within the first sale definition" and the Commission may decide "whether regulations were necessary to govern those transactions." 664 F.2d at 537. The Court is correct on that point, but even if it were not, the Commission cannot defeat Congressional NGPA pricing simply by defining "transfer for value" as not to include intra-corporate transfers, since there are still the sales to pipeline customers which qualify as "first sales".

[52] It is clear that a decision of a Court of Appeals may be affirmed where basis for affirmance exists, whether or not the Court of Appeals relied on that basis. That is even more obviously correct when, as here, the concept in question—the precise point at which the "first sale" occurs—does not create a practical difference. See

[Footnote continued on page 42]

no doubt, of course, that pipelines do transfer title to the gas which they produce. An infinitesimal portion is delivered "alone", in the "offsystem sales" which the FERC has classified as the only "first sales" of pipeline produced gas. But title to the rest of the pipeline produced gas is also transferred, by delivery to the pipeline's distributor, pipeline and end user customers, together with gas purchased by the pipeline. If transfer of *title* were to be viewed as a requirement for a "first sale", then those transfers of title of pipeline produced gas to the pipeline's major customers must be viewed as equally valid "first sales" as are the very small "off-system" sales which are recognized as "first sales" by the FERC. And they are much more significant in volume and in performance of the pipeline's public service duties.

Whether the "transfer" concept, or the concept that the "first sale" occurs when the gas is sold to the pipeline's customers, is used, the pipeline's total rates for its sales to its customers will be regulated on a cost of service basis by the FERC, as described in Section II B of this brief. Thus, whichever concept of place of sale is used, values consistent with NGPA prescribed prices will be included in the cost of service for pipeline produced gas, along with costs of transportation and sale, and the cost of purchased gas, to produce total resale rates. Under either concept, the consumers will pay the same amount.[53]

United States v. New York Telephone Co., 434 U.S. 159 (1977); Dandridge v. Williams, 397 U.S. 471 (1970); Helvering v. Lerner Stores Corp., 314 U.S. 463 (1941); Ryerson v. U.S., 312 U.S. 405 (1941); Letulle v. Scofield, 308 U.S. 415 (1940); United States v. American Railway Express Co., 265 U.S. 425 (1924).

[53] Petitioners have raised the red herring claim that if the point of "first sale" is conceptualized as being at the point of the sales to the pipeline's customers, "downline" (often hundreds of miles from the production area), the pipeline will not be able to collect its costs of transporting the gas to the market area, and its selling, general, administrative and financial costs. But that erroneous, and perhaps tongue in cheek, "concern" rests upon their refusal to acknowledge that the pipeline has the right, at minimum, to recover

[Footnote continued on page 43]

That is the important practical regulatory point. The important statutory interpretation point is that it is apparent that *all* gas produced by pipelines (and distributors) is the subject of a sale by the pipeline, so that the Court of Appeals' holding that *all* such gas is the subject of a "first sale" is fully supported by the "first sale" definition. The Court of Appeals' conclusion that such "first sale" takes place at the intracorporate transfer of such gas is clearly supportable, but the Decision of the Court of Appeals is also supportable on the basis of the sale to the pipeline's customers, the same result is created by either concept, and the Court of Appeals' reversal of the Commission can and should be affirmed on the basis of either concept.[54]

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all the costs in its overall cost of service pursuant to the Natural Gas Act (15 U.S.C. §§ 717, *et seq.*; see F.P.C. v. Hope Natural Gas Co., 320 U.S. 591 (1944), *et al.*), and *this case* concerns only what value the pipeline can include in that cost of service for its own produced gas. Petitioners nevertheless push on with their little joke, by suggesting that pipelines would be limited to NGPA prices for the gas they produce, plus only authorized "add ons" pursuant to Section 110 of the NGPA. Again, they err, because Section 110 does not purport to state *all* the costs that can be collected by a seller of gas: it merely says that the price limits of the NGPA will *not* be violated if the producer "adds on" appropriate amounts for performing the "production related" costs listed in Section 110. Pipeline transportation and other services outside the producing areas fall wholly outside Section 110, as Petitioners well know, and are recoverable under Sections 4 and 5 of the Natural Gas Act. Petitioner's "concern" is illusory. Finally, New York makes the incomprehensible claim (33, n. 31) that the downline sales point concept would interfere with importation of foreign gas at existing governmentally approved prices. That claim is in error because NGPA prices apply only to gas produced in the United States (as New York implicitly admits on page 31 of its brief) and because NGPA price ceilings only apply to gas itself: the total rates to be collected by pipelines for gas—domestic or foreign—delivered to the market areas are determined by the total pipeline cost of service—cost of gas purchased and produced by the pipeline, plus all other costs of transporting and otherwise doing business.

[54] Petitioners claim that because the "unless clause" refers to "such sale"—singular—being attributable to gas produced by the

[Footnote continued on page 44]

III. THE DECISION BELOW PRODUCES A JUSTIFIED RESULT

Petitioners repeatedly claim that pipeline producers will receive an "unjustified windfall" under the Decision below. That will be shown to be incorrect, below, but it must first be noted that such claims are also irrelevant. The issue here is what Congress *did*, not what the FERC or anyone else thinks it should have done. As the Court below stated:

> *It is not an agency's prerogative to alter a statutory scheme even if its alteration is as good or better than the congressional one.* The fact that the agency gives back all or part of what it takes from the law's grant in *no way justifies departure* from the congressional purpose in the first instance. 664 F.2d at 535-536. (emphasis added)

Petitioners apparently object to the method chosen by Congress to attempt to cure the natural gas shortage: the provision of higher Congressionally set price ceilings for all produced gas. But claims as to extra gas costs which

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pipeline, *all* of the gas in a *sale* must be such produced gas. They then reason that when a pipeline sells gas to its customers, it makes a "mixed sale" and only a portion of the gas is produced by the pipeline. But that is in error, because it is based upon the incorrect premise that a pipeline makes a *single* "sale" to each of its customers. In fact, however, while the sales are made to each customer pursuant to one or more *contracts*, there are a huge multiplicity of *sales*: each unit of gas is the subject of a separate *sale*, as it is delivered, in legal concept. Thus, each sale is made of a unit of purchased gas, or of pipeline produced gas, and each sale of pipeline produced gas is a "first sale", as explained above. That is the context in which Congress wrote the definition of "first sale", and it would have been incorrect to refer to a *portion* of a sale. The sale of each unit of gas occurs upon delivery (NPGA Section 2(22)), not upon the execution of the contracts. The contracts are executory, providing for title to pass later (Hatch v. Standard Oil, 100 U.S. 124, 131 (1879); 67 Am. Jur. 2d Sales § 6), leaving the risk of loss on the seller until the gas is produced and sold by transfer upon delivery. See, Public Service Electric & Gas Co. v. FPC, 371 F.2d 1 (3rd Cir. 1967) and U.C.C. §§ 2-106(1), 2-401 and 2-107: the sale of gas occurs after severance from the earth, when title to the then identifiable goods passes upon delivery.

will be created under the Decision of the Court below are not only speculation, at best, and unsupported by the record, but also go to legislative considerations which should have been—and were—presented to the Congress when the NGPA was being considered. But the NGPA was nevertheless enacted, because the Congress made the judgment that the goal of providing consumers a more ample and secure gas supply should be met by higher prices to producers. Thus, the successful attainment of a central purpose and anticipated result of the NGPA, *i.e.*, increased revenues to producers of gas, cannot legitimately be asserted by Petitioners as a reason for reversal by this Court of the Decision below.

The record does not provide support for the Petitioners' claims of the magnitude of the economic effect of the Decision of the Court below, and it is clear that the maximum cost of such Decision could produce is probably below 1% of the effect of the NGPA itself. This is because *all* pipeline produced gas constitutes only about 3% of total produced gas, but the FERC has voluntarily, in Order No. 98, ordered NGPA prices for the great bulk of the pipeline produced gas. The remaining gas, to which the FERC would deny NGPA prices, constitutes a small fraction of total pipeline produced gas, undoubtedly less than 1% of all gas affected by the NGPA. It is therefore ludicrous to suggest, as do some Petitioners, that the overall economy will be damaged, or national energy policy thwarted, by the Decision below. It is also likely that the increased pipeline production resulting from NGPA incentives, as described below, will provide economies by reducing use of more expensive alternative fuels by consumers.

The gas as to which the FERC efforts to deny NGPA pricing are thwarted by the Decision below is quite limited: it is gas produced from leases owned by pipelines, prior production from which leases was at some time valued on a cost of service basis for the gas itself. But such former cost of service treatment is not a distinguishing

feature, since independent and affiliate producers also produce gas from leases from which gas was produced when those companies, too, were being regulated on a cost of service basis: [55] but *all* production by *those companies* has been *admitted by the FERC* to be subject to NGPA pricing. Nevertheless, FERC Order No. 98 refuses to allow NGPA pricing as to such "formerly cost of service gas" *of pipelines only*, and Petitioners argue that NGPA pricing would be unfair, alleging that all costs of operating as to those leases were collected from customers in the past, which allegedly removed all production and marketing risk. But that is equally true—and sometimes equally untrue, see below—as to gas produced by independent and affiliate producers when they were regulated on an individual cost of service basis, and no one contends the NGPA does not apply to them. In fact, those producers frequently received *more* than their costs when the method by which they were regulated switched to the composite cost "area" and then "national" rate method: if they did not recover their costs, including successful and unsuccessful drilling costs, they could seek relief under the "special relief" provisions of the FERC regulations. 18 C.F.R. §§ 2.76 and 2.77. But Petitioners do not follow their own "logic" to contend that *those* producers should be denied NGPA prices: they limit their claims to pipelines.

It must be remembered that pipelines are seeking only the same price ceilings for all of the gas they produce as are applicable to all other producers, in each category of gas. Thus, if pipelines have "old gas" (Section 104, NGPA) for which other producers are allowed only the previous "national" rates set by FERC, plus cost of living escalations, that is all that pipeline producers would be allowed, too, for similar gas, under the Decision below. If pipelines cannot achieve such parity, their revenues

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[55] Such cost of service regulation was applied on an individual company basis to all producers originally, and the later "area and national rates" were based upon composite cost of service.

and capital will be less adequate, and they will be less able to compete for promising leases. Thus, Petitioners err in claiming that pipelines do not "need" NGPA pricing, because they will be allowed to recover their costs anyway. Such treatment would deny them the prices received by all other producers, and thus disadvantage them competitively.

Petitioners alternatively claim that "allowing" pipelines NGPA prices will not increase gas supply, alleging that pipelines will not—or could not—use the incentives provided by such prices anyway. This claim references the allegation that the gas for which the FERC would deny NGPA prices is gas produced from pre-1969 leases, from which increased production is allegedly not feasible. But those allegations are in error on at least four counts. First, increased production is often quite possible from old leases, by drilling to different, often deeper, horizons and/or additional drilling and reworking. But that is very expensive, and incentives of the NGPA pricing system are needed: indeed, a substantial motive for the NGPA was to provide incentives for such expensive drilling.[56] Second, increased revenues from *old* leases will provide capital to acquire and drill *new* leases. Third, it is not true that all gas for which the FERC would deny NGPA prices will be produced from "old" leases; some of it would be gas from newer leases, which the FERC would deny NGPA prices because gas from such leases was once priced on a cost of service basis only a few years ago, as a result of FERC approved settlements or other FERC orders. Finally, Petitioners' argument is that the subject incentives are useless as to "old leases", but the statutory interpretation which they urge on this Court would deny such incentives to gas from almost *all leases* owned by pipelines, as a matter of law. The FERC

[56] The NGPA also provides special prices for high cost "stripper wells", for which pipelines could qualify in some cases. In some such cases, a pipeline could receive higher revenues by the cost of service method than under the NGPA prices, but they are only seeking overall parity with other producers.

has now "granted" such incentives as to most pipeline produced gas, but the Congress did not know the FERC would do so when it passed the NGPA. Thus, to uphold the FERC interpretation, one must presume that Congress did not care if the FERC denied production incentives as to almost all pipeline production. And the FERC could still try to do that later, if it is held to have the "discretion" which its interpretation of the NGPA creates.[57]

It is also true that under the FERC position, some pipelines would be denied NGPA prices, even though they have had little true cost of service treatment in the past. Respondent Michigan Wisconsin, for example, received full cost of service treatment for only one year during nine years of pipeline production, and was already receiving area rates instead when the NGPA was passed. Further, nothing in the record indicates that cost of service pricing conferred the benefits claimed by Petitioners, and it does not necessarily convey benefits. For example, pipelines have been allowed lesser returns on equity then independent producers. Further, area or national rates, which were based on average costs, produced higher revenues than cost of service treatment for the companies with below average costs: the assumption that cost of service pricing is always higher is false. *See*, for example, *Nat'l Fuel Gas Supply Corp.*, F.P.C. Dkt. No. RP76-96, Opn. No. 58, 18 F.P.S. 5-829 (1979), where the FERC found that cost of service pricing provided *less* revenues than national rates.

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[57] At page 29, the FERC Brief concedes that: "To be sure, encouragement of pipeline exploration and production through incentive pricing would operate to increase the supply of gas in whichever market a pipeline operates." But despite that admission, and the fact that the Brief also admits, in the preceding paragraph, that pipeline gas is developed to serve the interstate markets for which the pipeline is responsible, the Brief then claims that pipeline produced gas is not significant: "only a secondary source of gas supply". That myopic attitude partly explains the motivation for the legal errors in the FERC Orders involved herein.

That latter fact also shows that Petitioners err when they make the sweeping claim that pipelines which once received cost of service pricing for gas they produced, as a result of which the FERC would now deny NGPA prices to such gas, *chose* to receive cost of service pricing. In some cases, such pricing was imposed by the FERC,[58] simply because of the age of the leases and/or wells. In other cases, it resulted from FERC refusal to allow a change from such pricing, and in other cases it resulted from FERC approved settlements. In only a few cases did it result from pipeline petition, and even then only after FERC approval. Nor was all pipeline production undertaken because of the promise of cost of service pricing. Many leases affected were acquired well before pipeline regulation existed.[59]

In short, the claims that pipelines are seeking, and would receive under the decision below, a "windfall", in violation of their prior "bargains", and all without providing any productive incentives for increased gas production, are in error. Thus, even if such claims were relevant, they are inaccurate. In fact, however, their very nature makes them irrelevant. The relevant fact is that Congress intended to, and did, apply NGPA pricing to pipeline produced gas, as a small part of its extensive efforts to correct the results of over thirty years of FERC policy, and the Court below was correct in refusing to allow the FERC to frustrate that action and intent.

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[58] See, *e.g.*, Colorado Interstate Gas Co. v. FPC, 324 U.S. 581, 600 (1945).

[59] Respondent Colorado Interstate Gas Company, for example, acquired Texas Panhandle properties ten years before the NGA, which still supply approximately 94% of CIG's company-owned pipeline production. *See Canadian River Gas Co., et al.*, 3 F.P.C. 32 (1942) *aff'd sub nom.* Colorado Interstate Gas Co. v. F.P.C., 324 U.S. 581 (1945). See also *Cities Service Gas Company*, 39 F.P.C. 1034, 1043, n. 14 (1968), for other companies which developed pipeline production without reference to cost of service treatment.

CONCLUSION

The thorough opinion of the Court below clearly reaches the appropriate result, pursuant to the language, purpose and legislative history of the NGPA. Under that result, consumers will be fully protected, including by continued FERC regulation of interstate pipeline rates (and state regulation of intrastate and distributor rates). All that changes is that the NGPA producer prices controls for the gas itself apply to *all* gas, which is exactly what Congress intended.

Accordingly, it is respectfully requested that the Decision below be affirmed, or that these proceedings be dismissed on the basis that certiorari has been unnecessarily granted.

Respectfully submitted,

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January 11, 1983

APPENDIX

S. 2104, as passed by the Senate on Oct. 4, 1977, 95th Cong., 1st Sess. (1977), 123 Cong. Rec. S16325, Sections 205 and 206.

Sec. 205. Section 4(e) of the Natural Gas Act (15 U.S.C. 717c(e)) is amended by adding at the end thereof the following new sentence: "Notwithstanding the foregoing, the Commission shall have no power to deny, in whole or in part, any rate or charge made, demanded, or received by any natural-gas company for, or in connection with, the purchase or sale of natural gas, or that portion of the rates and charges of such natural-gas company which relates to such purchase or sale, except (A) to the extent that such rates or charges, or such portion thereof, for new natural gas sold or delivered from offshore Federal lands exceed the national ceiling or interim ceiling established or modified by regulation of the Commission pursuant to section 24 of this Act or (B) in any case where a natural-gas company which transports natural gas in interstate commerce purchases new natural gas from an affiliate or produces new natural gas from its own properties, to the extent that the Commission determines that the rates and charges therefor exceed the current rates and charges, or portion thereof, made, demanded, or received for comparable sales by persons not affiliated with such natural-gas company.".

Sec. 206. Section 5(a) of the Natural Gas Act (15 U.S.C. 717d(a)) is amended by striking the period at the end thereof and by adding the following: ": Provided further, That the Commission shall have no power (1) to deny, in whole or in part, any rate or charge made, demanded, or received by any natural-gas company for, or in connection with, the purchase or sale of new natural gas, or that portion of the rates and charges of such natural-gas company which relates to such purchase or sale except (A) to the extent that such rates or charges, or such portions thereof, for new natural gas sold or de-

livered from offshore Federal lands exceed the national ceiling or interim ceiling established or modified by regulation of the Commission pursuant to section 24 of this Act, or (B) in any case where a natural-gas company which transports natural gas in interstate commerce purchases new natural gas from an affiliate or produces new natural gas from its own properties, to the extent that the Commission determines that the rates and charges therefor exceed the current rates and charges, or portion thereof, made, demanded, or received for comparable sales by persons not affiliated with such natural-gas company; or (2) to order a decrease in the rate or charge made, demanded, or received for the sale or transfer of old natural gas or new natural gas produced from offshore Federal lands by a natural-gas company if such rate or charge has been previously determined or deemed to be just and reasonable pursuant to this Act.".

Henry M. Jackson, Wash., Chairman
Frank Church, Idaho
J. Bennett Johnston, La.
James Abourezk, S. Dak.
Floyd K. Haskyll, Colo.
Dale Bumpers, Ark.
Wendell H. Ford, Ky.
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D. Michael Harvey, Chief Counsel
W. O. Craft, Jr., Minority Counsel

UNITED STATES SENATE

COMMITTEE ON
ENERGY AND NATURAL RESOURCES

Washington, D.C. 20510

June 6, 1978

MEMORANDUM

To: Senate Conferees on Natural Gas

From: Senator Henry M. Jackson

Re: Remaining Natural Gas Conference Issues

At the May 24 Conference Committee meeting the staff was directed to meet to develop suggestions for resolving the remaining natural gas conference issues.

The enclosed agenda covers all of the natural gas conference issues that were not addressed by the compromise proposal. Both the House and Senate positions on each issue are summarized and a staff recommendation is included for each issue except natural gas storage facilities.

The agenda will be covered at the Conference Committee meeting on Wednesday, June 7, 1978 at 2:00 p.m. in Room 2123 Rayburn House Office Building.

Questions concerning the agenda should be addressed to Betsy Moler, Staff Counsel, at extension 40611.

AGENDA

Natural Gas Conference Committee

June 7, 1978

Subjects Not Addressed by the Compromise Proposal Previously Adopted

Subject	Page
I. Pipeline Regulation and Pass Through of Price Increases	1
A. Pass Through of Wellhead Price Increases by Interstate Pipelines	1
B. Prohibition on Indirect Wellhead Price Regulation Via Pipeline Certificate Requirements	1
C. Natural Gas Curtailment Policy	2
1. Essential Agricultural Uses	2
(a) Priority	2
(b) Definitions	2
(i) Agricultural Uses	3
(ii) High Priority Uses	3
(c) Role of the Secretary of Agriculture	4
(d) Scope	4
2. Industrial Uses (other than as boiler fuel)	5
3. Application for Special Relief	5
4. Limitation on Boiler Fuel Curtailment	5
II. Supplemental Authorities	6
A. Natural Gas Act Exemption for Certain Sales	6
B. Transportation and Sale Authority	7
C. Contractual Prohibitions on Commingling	8
D. Synthetic Natural Gas	9
E. Natural Gas Storage Facilities	9

3a (continued)

Subject	Page
III. Administrative Procedure, Enforcement; and Judicial Review	10
A. Administrative Procedure	10
B. Judicial Review	10
C. Enforcement	11
1. Civil Penalties	11
2. Criminal Penalties	12
D. Information	12
1. Required Studies	12
2. Authority to Obtain Information	13
IV. Indian Lands	13

I. Pipeline Regulation and Pass Through of Price Increases

A. Pass Through of Wellhead Price Increases by Interstate Pipelines

House Provision:

Guarantees that interstate pipelines may pass through costs of natural gas purchases if the price of the purchased natural gas does not exceed the ceiling price levels established under the legislation. Natural gas prices equal to or less than the applicable natural gas ceiling prices established under the legislation are deemed "just and reasonable" for purposes of the Natural Gas Act.

[Section 417(a) and (b) respectively amending sections 4(a) and 5(a) of the Natural Gas Act; pages 40-41.*]

Senate Provision:

Guarantees that interstate pipelines may pass through costs of new natural gas purchases if the price of the purchased natural gas does not exceed:

(1) in the case of natural gas sold from offshore Federal lands, the applicable ceiling prices; and

(2) in the case of sales between affiliated entities, the price received in comparable transactions by persons not affiliated with the pipeline.

[Sections 205 and 206 respectively amending sections 4(e) and 5(a) of the Natural Gas Act; pages 40-41.]

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* Page references are to Comparative Print, dated November 28, 1977.

Staff Recommendation:

Adopt House provision until date of deregulation. Thereafter use Senate provision modified to read:

Guarantee that interstate pipelines may pass through costs of deregulated natural gas purchases. In the case of transactions between affiliates, guarantee pass through if the price of the purchased natural gas does not exceed the price received in comparable transactions by persons not affiliated with the pipeline in the case of sales between affiliated entities.

B. Prohibition on Indirect Wellhead Price Regulation Via Pipeline Certificate Requirements

House Provision:

FERC may not deny a certificate of public convenience and necessity to an interstate pipeline based upon the price of natural gas if the price does not exceed the applicable ceiling price.

Petitioner's Reply Brief

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Nos. 81-1889, *et al.*

Office - Supreme Court, U.S.
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ALEXANDER L. STEVAS,
CLERK

IN THE

Supreme Court of the United States

October Term, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*

Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*

Respondents.

ON WRIT OF CERTIORARI TO THE COURT OF APPEALS FOR THE FIFTH CIRCUIT

REPLY BRIEF OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

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Gray v. *Powell*, 314 U.S. 402 (1941) 7

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Pennsylvania Railroad Co. v. *International Coal Mining Co.*, 230 U.S. 184 (1912) 9

Permian Basin Area Rate Cases, 390 U.S. 747 (1978) 4

Phillips Petroleum Co. v. *Wisconsin*, 347 U.S. 672 (1954) 12

Posades v. *National City Bank*, 296 U.S. 497 (1936) 3

Rubin v. *United States*, 449 U.S. 424 (1981) 7

United Gas Improvement Co. v. *Continental Oil Co.*, 381 U.S. 392 (1965) 7

United Gas Pipeline Co. v. *Mobile Gas Service Corp.*, 350 U.S. 32 (1956) 4

United States v. *United Continental Tuna Corp.*, 425 U.S. 164 (1976) 3

STATUTES:

Natural Gas Act, 15 U.S.C. §§717, *et seq.*:
Section 7, 15 U.S.C. § 717f 2,6

Natural Gas Policy Act of 1978, 15 U.S.C. §§3301 *et seq.*:
Section 2(20), 15 U.S.C. §3301 (20) 6, 4
Section 2(21), 15 U.S.C. §3301 (21) ..... *passim*
Section 101(b) (9), 15 U.S.C. §3311 (b) (9) 5
Section 203, 15 U.S.C. §3343 ..... 10, 11
Section 601(b) (1) (E), 15 U.S.C.
§3431 (b) (1) (E) ..8, 9, 10

LEGISLATIVE HISTORY:

H.R. Rep. No. 1752, 95th Cong.
2nd Sess. (1978) 5

124 Cong. Rec. H. 13, 117 (daily ed. Oct. 14, 1978) 5

MISCELLANEOUS:

Statistics of Interstate Pipeline companies, 1979,
U.S. Dept. of Energy (October 1980) 12

IN THE

Supreme Court of the United States

October Term, 1981

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*

Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*

Respondents.

ON WRIT OF CERTIORARI TO THE COURT OF APPEALS FOR THE FIFTH CIRCUIT

REPLY BRIEF OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

The Public Service Commission of the State of New York (New York), a petitioner in this consolidated case, herewith files its brief in reply to the answering briefs filed by Mid-Louisiana Gas Company, *et al.* (Mid-Louisiana), Consolidated Gas Supply Corporation (Consolidated), and Michigan Wisconsin Pipe Line Company (Michigan Wisconsin), respectively.[1]

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[1]In this brief, references to the opening brief filed by New York are given as "(N.Y., _____)," and references to the briefs filed by the respondents as "(Mid-Louisiana, _____)," "(Consolidated, _____)" and "(Michigan Wisconsin, _____)," respectively. References to the Appendix to the Petition for Certiorari in No. 81-1889, which by order of the Court serves as the record of the case in the court below, are listed as "(P.A. _____)"

ARGUMENT

The briefs filed by the respondent pipelines start from the premise that Congress intended the Natural Gas Policy Act (NGPA), 15 U.S.C. §§3301, *et seq.*, to supersede all Commission regulation of gas production activities under the Natural Gas Act, 15 U.S.C. §§717, *et seq.* On this assumption, they argue that the language of the NGPA should be construed as affording all pipeline production of natural gas the maximum lawful ceiling prices set forth in Title I of the NGPA for the "first sales" of natural gas. As made clear in New York's opening brief, the underlying premise is erroneous and the language, structure, and legislative history of the NGPA do not lend themselves to any such construction.

1. A primary difficulty with the respondents' approach is the absence of anything in the language or history of the NGPA which expresses any Congressional intent to repeal the Commission's authority under the Natural Gas Act over the production operations of interstate pipelines, authority which it had exercised throughout the forty years of regulation under the Natural Gas Act. Respondents have been unable to point to a single situation during the two years in which the NGPA was under active consideration in which they or any other person expressed dissatisfaction with the existing regulation of pipeline production, or stated that the maximum lawful ceiling rates of Title I of the NGPA were to apply to all pipeline production.[2] Instead, they are forced to rely on isolated language in the reports and debates as to the comprehensive nature of the proposed legislation and on the argument that there are no express

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[2]The one arguable exception is a statement, by an ex-employee of the Commission who strongly opposed any legislation, that the bill being considered by the House Committee, which contained no definition of "sale" or "first sale," would have resulted in pipeline windfalls. It is, however, axiomatic that such statements by opponents of legislation are not persuasive of Congressional intent even when made by persons far more closely involved in the drafting of the legislation. See, *e.g.*, *NLRB* v. *Fruit & Vegetable Packers*, 377 U.S. 58, 66 (1964).

statements of an intent to exclude pipeline production from eligibility for the Title I ceiling prices.

Established statutory authority cannot be swept aside by this type of showing. The issue, despite respondents' efforts to disguise it, is repeal by implication. To the extent this is ever permissible,[3] it cannot be accomplished by a combination of generalization and negative inference.

Specifically, Congressional intent cannot be inferred on the basis of a presumed Congressional ignorance of the differences between pipeline and producer regulation under the Natural Gas Act. As New York detailed in its opening brief, regulation of pipeline production operations under the Natural Gas Act not only followed different administrative and judicial paths from the regulation of sales by independent producers, but involved substantive distinctions bearing directly upon the perceived need for legislative change which led to the enactment of the NGPA.

Under the area or nationwide ceiling rates prescribed for sales of gas by producers *to* interstate pipelines, revenues resulted only to the extent gas was produced and sold. The risk of complete failure or inadequate revenues always existed as a damper upon optimum production operations. There was a general consensus that the inadequacy of the area and nationwide rates established under the National Gas Act, coupled with the Federal Power Commission's lack of authority over the rates for intrastate and direct industrial sales by producers, had been largely responsible for curtailment of pipeline deliveries of gas in the mid-1970's. In contrast, pipeline production priced on an individual company cost-of-service basis presented no such problems: the pipeline was ensured of a reasonable return on its prudent investment regardless of the success of its efforts or the ultimate cost of producing natural gas.

The distinction was a real one and cannot be covered over by arguments that both pricing techniques were "cost

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[3]But see *Posades* v. *National City Bank*, 296 U.S. 497, 503 (1936); *United States* v. *United Continental Tuna*, 425 U.S. 164, 168 (1976).

based"[4] or that "dry hole" costs were included in the nationwide or area rates available to the producers. The differences were well recognized by the pipelines themselves. Thus, the respondent Consolidated, which now attempts to minimize the lack of risk it enjoys on its older gas priced on a cost-of-service basis (Consolidated, 24), was arguing as late as 1977 that unless cost-of-service treatment was extended to its new production it would not be able to invest the sums necessary for an optimum production effort on behalf of its customers, and that it was prepared to adhere to such cost-of-service treatment even if the area or nationwide rates for independent producers subsequently rose to levels in excess of its costs. See Consolidated's Brief on Exceptions in Docket Nos. RP73-107, *et al.*, filed February 28, 1977, pp. 2, 9.[5]

Another significant distinction under the Natural Gas Act between the regulation of producer sales to interstate pipelines and regulation of the costs of production operations conducted by the pipelines themselves, was that the price for producer sales to pipelines was also limited by the gas sales contract[6] whereas no such contractual

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[4]The fact that the area and nationwide ceiling prices fixed by the Commission for producer sales to interstate pipelines were primarily based on average producer costs did not, of course, mean that each producer would recover all of its costs, plus a reasonable return, regardless of the success of the venture. That they would not do so in many cases was one of the major producer objections to the Commission's area rates. See *Permian Basin Area Rate Cases*, 390 U.S. 747, 813–21, 825–28 (1978).

[5]As indicated at p. 35 of New York's opening brief, similar arguments were being made by Columbia Gas Transmission Corp. and the respondent Kansas-Nebraska Natural Gas Company.

[6]See *United Gas Pipeline* v. *Mobile Gas Service Corp.*, 350 U.S. 32 (1956). While the Commission retained limited powers to set aside contractual limitations where it could find the public interest so required, *see FPC* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956); *Permian Basin Area Rate Cases, supra*, 390 U.S. at 820-21, this authority could not serve as a positive restraint upon any costs which would be imputed to a pipeline's own production under ceiling price regulation.

limitations were applicable in the case of a pipeline's own production. As a consequence, the contracting process could not serve, as in the case of the sales by independent producers, to control the terms of sale or reduce the price of pipeline production below the first sale maximum "ceiling" price levels where market forces so indicated. Nor could the contracting process serve as a limitation on price levels for pipeline production after various categories of natural gas were deregulated pursuant to the schedule prescribed in Section 121 of the NGPA. Yet, as the draftsmen of the Act stressed, such contractual limitations upon excessive prices, as expressly recognized in Section 101(b)(9) of the Act, were intended to play an important role in the regulatory scheme adopted by the Congress. See, *e.g.*, Conference Report on the NGPA, H. R. Rep. No. 1752, 95th Cong., 2nd Sess. (1978) p. 74; Explanation Statement of Representative Dingell, 124 Cong. Rec. H. 13,117 (daily ed. October 14, 1978).

2. Given these basic distinctions between the pre-existing regulation of pipeline production and producer sales to pipelines, any showing that the language, structure and history of the NGPA compelled a result different from that contemporaneously adopted by the agency entrusted with the administration, interpretation and enforcement of the new Act (and most familiar with the prior regulatory structure) would have to be far stronger than that set forth in the opinion below or in the briefs of the pipeline respondents. The Commission's construction of Section 2(21) of the Act as covering pipeline production only to the extent it is the subject of discrete sales by the pipelines analogous to the wellhead sales by separate production companies is fully consistent with the language of the Section and the legislative history of the Act. The fact that it results in maintenance of the regulatory status quo with respect to pipeline production which is not sold off-system but remains a fungible part of system supply, with the question of how the various categories of pipeline production should be priced remaining a matter for

Commission determination under the Natural Gas Act, does not in anyway detract from the validity of the Commission's construction.

The Court of Appeals, in reaching a contrary opinion, found it necessary to impute a sale to the intracorporate transfer of gas within the pipeline prior to sale of pipeline produced gas together with gas acquired from producers and other pipelines. As New York demonstrated at pages 25–26 of its opening brief, such intracorporate transactions cannot properly be classified as sales within the definition of that term in Section 2(20) of the Act and is inconsistent with the prior administrative construction of the sales requiring certification under Section 7 of the Natural Gas Act. The briefs for the pipeline respondents completely fail to respond to those arguments.

Consolidated, whose primary position is that Section 2(21) is clear upon its face and the nature of a first sale is therefor irrelevant, does not bother to mention Section 2(20) or petitioners' arguments relating thereto. Michigan Wisconsin addresses the issue by denying its existence. In its view, any discussion of where any "first sale" of pipeline production takes place is without significance because "the focus of the 'first sale' concept is not upon a 'sale' but upon its use as a drafting mechanism for identifying the producer of gas." (Michigan Wisconsin, 38).[7]

Only the Mid-Louisiana brief attempts to support the Court of Appeals' opinion on its own terms. Its efforts to fit the intracorporate transfer within the statutory definition of a sale are, however, unpersuasive. It cites several cases for the proposition that sales will be found to exist where "all of the traditional attributes associated with the term" are not present (Mid-Louisiana, 23–24). But these cases either

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[7]Michigan Wisconsin solemnly assures the Court that, if it desires to "conceptualize" the term first sale in the context of the Act's definition of a sale, undisclosed "compelling reasons" exist for equating a "transfer of possession" of pipeline production with a "transfer for value," despite the absence of either consideration or any transfer of title. (Michigan Wisconsin, 40).

involved other statutory terms and definitions found to be controlling[8] or presented questions other than the existence of a sale.[9] Mid-Louisiana also argues that, while no transfer of title occurred as part of the imputed intracorporate "sale," there was a genuine "transfer for value" (Mid-Louisiana, 25). But no consideration, monetary or otherwise, between the purported "buyer" and "seller" is claimed. Instead, it is asserted that the physical transfer of gas between divisions of the pipeline triggers the obligation of the pipeline to pay royalties and subjects the pipeline to Commission regulation. Assuming these wholly unsupported claims are valid,[10] they do not show a transfer of value from one division of the pipeline to another. In short, none of the respondents have shown how the court of appeals' imputation of a sale within the pipeline is consistent with the definition of "sale" incorporated into the Act. The failure is equally applicable to any other "point of transfer" to which a sale conceivably could be imputed.

3. The pipeline briefs also fail to meet New York's arguments showing the incompatability of the lower court's ruling with various other sections of the NGPA. Thus, New

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[8]*Gray* v. *Powell*, 314 U.S. 402, 416 (1941). (Statute provided for tax on sale or "other disposal" of coal; transaction found to be a "disposal"). *Rubin* v. *United States*, 449 U.S. 424, 428-430 (1981) ("Sale" defined to include "disposition of interest in a security;" pledge of stock held to be such a "disposition.")

[9]*United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392 (1965) (Issue was whether admitted sale of gas lease was a sale of "natural gas.")

[10]There is no basis for assuming the transfer of gas from the production to the transportation personnel of the pipeline is related to the royalty payment obligation, which is normally tied either to the gas' production or its subsequent sale. Similarly, the Commission's jurisdiction under the Natural Gas Act over the cost of pipeline production taken into system supply, which was established long before its jurisdiction over sales to the pipelines by producers, is not tied to the physical transfer of the gas to the pipeline's transmission divisions. See *Canadian River Gas Co.* 3 F.P.C. 32 (1942), affirmed *sub nom. Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945).

York pointed out (N.Y., 20–21, 27) that Congress in Section 601(b) (1) (E) of the Act limited the passthrough provisions of the Act in the case of first sales between affiliates, but provided no such protection for pipeline production, though such protection had been included in the Senate version of the bill which had expressly covered new pipeline production. Respondents' attempt to circumvent this embarrassing omission by arguing that, since Section 601(b) (1) (E) applies to "any first sale between any interstate pipeline and any affiliate of such pipeline," it covers the price which a pipeline can charge its distribution affiliates for its gas production. Alternatively they argue that the legislative history of Section 601(b) (1) (E) shows that the language adopted was intended to apply to all pipeline production. Neither argument has any semblance of validity.

The first proposition assumes the answer to the issue before the Court since the section applies only to "first sales." Moreover, the argument would not apply in the case of those respondents (including El Paso Natural Gas, Kansas-Nebraska, Mid-Louisiana and Colorado Interstate) which do not sell gas to distribution affiliates. Any consumer protection would, in any event, be non-existent with respect to pipeline production sold to non-affiliated distributors—in the case of Consolidated, all of its customers in New York State.[11]

The other pipeline argument is based upon a document of June 6, 1978 prepared by members of the Senate Committee staff setting forth the agenda of matters to be discussed by the conferees on the legislation which resulted in the

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[11]It is far from clear that the affiliated distributors would secure any real protection where non-affiliated distributors paid ceiling prices for the gas they purchased from the pipeline or some other pipeline. However, the court need not consider this question since, obviously, Congress did not intend to provide affiliated distributors with greater protection than distributors not affiliated with a pipeline.

NGPA. See Michigan Wisconsin Br. 2a–4a. The cited language in the staff document purports to paraphrase the passthrough language of the bills which had been adopted by the House and Senate and recommends that the House provision (which had not referred to the affiliate problem) be adopted "until date of deregulation" and thereafter a "modified" version of the Senate provision be utilized. The pipelines' argument appears to be that since the paraphrase of the language of the Senate bill passthrough language in the staff document is similar to the language proposed by the staff for adoption after deregulation as well as to that contained in Section 601(b) (1) (E), the latter must be construed as applying to all pipeline production because the Senate bill had applied to pipeline production as well as to sales between affiliates.

The argument is a classic example of why this court has consistently rejected attempts to illuminate allegedly ambiguous statutory language through peripheral legislative history involving non-public documents prepared by secondary actors. See, *e.g.*, *Pennsylvania Railroad Co.* v. *International Coal Mining Co.*, 230 U.S. 184, 198–99 (1912). Nothing in the cited language indicates that the draftsmen of the staff report intended to include all pipeline production in the gas to be afforded the statutory ceiling rates, or believed that the conferees had previously so agreed. Instead, the Court is asked to infer such an intent from the approximation of the language used to describe the Senate bill's passthrough provisions with the recommended language for inclusion in the final legislation.

This would be an extremely questionable use of legislative history even if we were dealing with the Conference Report on the Act itself, rather than a report prepared by undisclosed staff personnel for the benefit of the conferees during the course of their consideration of the legislation. Moreover, the staff report recommends language never adopted which would have been applicable only to gas already deregulated, and which in several other significant

respects does not track the language of Section 601(b) (1) (E) it allegedly illuminates. Thus, unlike Section 601(b) (1) (E), the recommended language makes no reference to "first sales" (a concept which had appeared in the house passed bill and was carried forward into the NGPA, but was not in the Senate bill) and refers to inter-affiliate "transactions" (which arguably encompass the pipeline production which had been covered by the Senate bill) rather than "sales" which have a more limited meaning. (See N.Y. Br., pp. 25–26). In short, even on its own terms, the June 6, 1978 staff report does not show that the passthrough provisions of the Act are limited with respect to pipeline production sold to non-affiliated customers. Finally, New York notes that the June 6, 1978 agenda as reproduced by respondents was apparently never placed before the conferees but instead was replaced by an errata sheet.

4. New York also demonstrated in its opening brief (pp. 30–31) that, contrary to the view of the court below, the special provision of Section 203(b) (2) of the Act authorizing the Commission to determine by rule the "first sale acquisition cost" of pipeline production for purposes of the incremental pricing provisions of Title II of the Act, makes sense only in the context of a Congressional understanding that some pipeline production would not involve a "first sale" since the first sale acquisition cost for "first sales," is specified in Section 203(b) (1) (A). Consolidated does not respond to our argument, confining itself to a repetition of the Court of Appeals' contrary position (Consolidated, 11). Michigan Wisconsin suggests that Section 203(b) (2) was required, despite the fact that all pipeline productioin assertedly involves a "first sale," because "Congress knew that there is no 'price paid' when a pipeline acquires gas which it produces itself" and Section 203(b) (1) (A) defines the first sale acquisition cost for any first sale as the "price paid" for the gas (Michigan Wisconsin, 18, n.20). Aside from the circularity of the argument (pipeline production involves first sales for which no price is paid), it is invalid on

its own terms; if all pipeline production involves a first sale, the "price paid" for the gas by a pipeline's customers could be computed from the first sale price the pipeline is authorized to collect under the NGPA and no special determination by the Commission would be required.

Finally, the Mid-Louisiana brief contends (p.21, n.14) that "if...pipeline production is not the subject of a 'first sale' such production would not qualify for incremental pricing under the NGPA because Section 203(a) requires incremental pricing of only the "first sales" of domestic production...." In fact, however, Section 203(a) is not so limited. Instead, it requires the passthrough to the gas consumers subject to incremental pricing of "any portion of the first sale acquisition cost" above specified levels with respect to *all* new, rollover, high-cost and stripper-well production, as well as other categories of gas which admittedly do not qualify as "first sales." It was because the first sale acquisition cost concepts applied to pipeline production not eligible for first sale treatment and the "price paid" could thus not otherwise be determined, that it was necessary to provide in Section 203(b) (2) that such cost be determined by the Commission.

5. There is no merit to the pipelines' argument that the different treatment allegedly provided by the Commission in Order No. 58 to pipeline affiliate production, as contrasted with that of the pipeline itself, shows that the Commission has "elevate[d] corporate form over substance." On the contrary, the distinction made by the Commission reflects the pre-existing differences between the two types of production, as well as avoiding unnecessary windfalls in the pipeline production situation.[12]

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[12]The pipeline respondents are unable to argue that the much higher prices they would secure under the court of appeals' opinion for their gas presently priced on a cost-of-service basis is necessary to induce optimum production efforts with respect to such gas since they will secure a return of, and on, any investment required to enhance this production. They accordingly attempt to downplay the impact of the

As made clear in New York's opening brief, the distinction between the treatment of pipeline and affiliate production is not an artifice developed by the Commission in Order No. 58 to achieve a particular objective but, instead, an extension of a dichotomy going back to the beginnings of regulation under the Natural Gas Act. Pipelines have had the choice of conducting their own production subject to regulation on a virtually risk-free cost of service basis or establishing separate production affiliates operated like independent producers and subject, after this Court's *Phillips* decision,[13] to regulation like, and the risks of independent producers.

The Commission's determination in Order No. 58 that affiliate production companies qualified for the maximum lawful ceiling prices prescribed by Title I of the NGPA reflected the jurisdictional fact that all of the sales of the gas sold to pipelines by separate but affiliated production companies are from discrete wells owned by the affiliated producer and thus involve sales of gas "attributable to the volumes of gas produced by such . . . affiliate." This is a very

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resulting cost increases by emphasizing the small percentage of total pipeline gas supplies attributable to pipeline production. (See, *e.g.*, Consolidated. App. D.). The $181,257,326 figure given in Appendix A of the Commission's Reply Memorandum on Certiorari does not include non-respondent companies with their own production; *e.g.*, Columbia Gas Transmission Corporation, where repricing its old cost-of-service production at NGPA levels results in an approximate $125,000,000 annual increase, and National Fuel Gas Supply Corporation . The consequent price increases of well over $200,000,000 annually would be significant if spread evenly throughout the country. The impact, however, is concentrated upon the customers of the relatively few pipelines with their own production. Thus, as of 1979, pipeline production accounted for 79% of Kentucky-West Virginia's total gas supply. See *Statistics of Interstate Pipeline Companies, 1979*, U.S. Dept. of Energy (October 1980). While this is an extreme case, approximately 16% of the total gas supply of both El Paso and Mid-Louisiana was their own production and the figures for Colorado Interstate and Kansas-Nebraska were approximately 13.5%.

[13] *Phillips Petroleum Company* v. *Wisconsin*, 347 U.S. 672 (1954).

different situation than that applicable to the bulk of a pipeline's own production which is sold as a fungible part of the pipeline's system supply along with the gas purchased from producers or other pipelines. It is, we suggest, anomalous for the respondents to assert, on the one hand, that the Commission's construction of Section 2(21) (B) must be erroneous because the small percentage of pipeline production qualifying as a first sale under the Commission's interpretation would effectively read the "unless clause" out of the section, while ignoring the substantial volumes of affiliate gas qualifying thereunder.

CONCLUSION

For the reasons set forth herein, and in New York's opening brief, the judgment of the Court of Appeals should be reversed.

Respectfully submitted,

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OF THE STATE OF NEW YORK

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Petitioner's Reply Brief

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Nos. 81-1889, 81-1958,
81-2042 and 82-19

IN THE

Supreme Court of the United States

October Term, 1982

PUBLIC SERVICE COMMISSION
OF THE STATE OF NEW YORK;
ARIZONA ELECTRIC POWER COOPERATIVE, INC.;
STATE OF MICHIGAN; AND
FEDERAL ENERGY REGULATORY COMMISSION,
Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

**ON WRIT OF CERTIORARI
TO THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT**

REPLY OF ARIZONA ELECTRIC POWER COOPERATIVE, INC. TO BRIEFS FOR RESPONDENTS

No. 81-1958

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TABLE OF CONTENTS

Page

TABLE OF CONTENTS i

TABLE OF AUTHORITIES ii

INTRODUCTION 1

ARGUMENT 2

I. Respondents Have Not Rebutted AEPCO's Contention That The Court Of Appeals Has Effected An Unlawful Repeal By Implication Of A Portion Of The Natural Gas Act 2

II. Respondents Have Made No Effective Rebuttal To AEPCO's Arguments That The Interpretation Of The Term "First Sale" By The Court Below Is Erroneous 6

III. Respondents Have Not Disproved AEPCO's Thesis That The Decision Below Promotes Inequity 7

CONCLUSION 8

TABLE OF AUTHORITIES

CASES

Colorado Interstate Gas Co. v. FPC, 324 U.S. 581 (1945) 3

Columbia Gas Development Corp. v. FERC, 651 F.2d 1146 (5th Cir. 1981) 6

Commissioner of Internal Revenue v. Brown, 380 U.S. 563 (1965) 4

STATUTES

Natural Gas Act, 15 U.S.C. §§ 717 *et seq.* ..... *passim*
Section 4, 15 U.S.C. 717c 2, 4, 6
Section 5, 15 U.S.C. 717d 2, 4
Natural Gas Policy Act, 15 U.S.C. §§ 3301 *et seq.* .. *passim*
Section 2(20), 15 U.S.C. 3301 (20) 6
Section 2(21), 15 U.S.C. 3301 (21) 5, 7
Section 501(a), 15 U.S.C. 3411 (a) 6
Section 501(b), 15 U.S.C. 3411 (b) 6
Section 601(b) (1) (E), 15 U.S.C. 3431 (b) (1) (E) . 3, 4
Section 601(c) (2), 15 U.S.C. 3431 (c) (2) 4

REGULATIONS

Order No. 58, Docket No. RM80-7 (issued November 14, 1979) 5, 6

Order No. 98, Docket No. RM80-6 (issued August 4, 1980) 2, 6

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REPLY OF ARIZONA ELECTRIC POWER COOPERATIVE, INC. TO BRIEFS FOR RESPONDENTS

Arizona Electric Power Cooperative, Inc. (AEPCO), petitioner in Case No. 81-1958, herewith replies to the various briefs filed by respondents Mid-Louisiana Gas Company, *et al.* (Mid-La)[1], Consolidated Gas Supply Corporation (Con Gas) and Michigan-Wisconsin Pipeline Company (Mich-Wis) in the above identified proceedings.

INTRODUCTION

The briefs filed by the pipeline respondents are, in AEPCO's opinion, noteworthy for the paucity of their

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[1]Respondents Mid-Louisiana Gas Company, El Paso Natural Gas Company, Colorado Interstate Gas Company, Kentucky-West Virginia Gas Company, and Kansas-Nebraska Natural Gas Company filed a joint brief.

references to specific arguments of AEPCO.[2] Moreover, the respondents have evaded specific replies to the points raised by the other petitioners and have instead grouped all responses to petitioners' arguments together.

More fundamentally, the respondents' briefs are directed overwhelmingly towards the question of what constitutes a statutory "first sale" under the Natural Gas Policy Act (NGPA). Their briefs essentially ignore the *independent and simpler* basis for decision which AEPCO has presented, *i.e.*, whether the decision of the Court of Appeals constitutes an unlawful implied repeal of the provisions of the Natural Gas Act (NGA) which authorize the Federal Energy Regulatory Commission (Commission) to fix rates for pipeline produced natural gas. In AEPCO's opinion, this is the crucial issue in this case, and it is of the utmost significance that the respondents have scarcely tried to rebut our arguments on this issue.

In addition, AEPCO made certain unique arguments concerning the statutory definition of a "first sale" in light of the "unless" clause, the teachings of the legislative history of the NGPA as to whether an intracorporate transfer is a first sale, and the application of the wrong standard for judicial review by the Court below. Finally, AEPCO alone argued that even if the decision of the Court below as to intracorporate transfers of pipeline produced gas is correct, that Court erred in failing to remand the case to the Commission rather than in vacating that agency's Order 98. None of these arguments have been addressed by our opponents.

ARGUMENT

I. Respondents Have Not Rebutted AEPCO's Contention That The Court Of Appeals Has Effected An Unlawful Repeal By Implication Of A Portion Of The Natural Gas Act.

1. AEPCO argued (Br., pp. 14-15) that Sections 4 and 5 of the NGA grant the Commission the power to fix just and

[2]There are only six specific references to AEPCO's brief in all three Respondents' briefs taken together.

reasonable rates for pipelines. Such power has always been held to include the fixing of rates for a pipeline's own production on a cost-of-service basis. *Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945). The NGPA does not expressly repeal this NGA authority of the Commission. If it did, respondents would have quoted the pertinent text of that Act rather than burdening the Court with convoluted and lengthy arguments trying to explain how the NGPA has repealed this aspect of the NGA. Instead of answering the merits of AEPCO's extensive legal arguments on this issue (Br., pp. 14-25), Mid-La (Br., p. 42) and Mich-Wis (Br., p. 13, ftn. 14), simply recite the wholly unsupported and self-serving conclusion that the express language of the NGPA repeals the Commission's jurisdiction to regulate pipeline production under the Natural Gas Act.

The Court of Appeals did not find that there had been an express repeal; rather it found that there was an implied repeal without specifying any evidence of the necessary "clear and manifest" Congressional intent to repeal, or showing any irreconcilable conflict between the two statutes. Here, there is *no* evidence of either. In fact, the Court below made no findings on the issue of an implied repeal and clearly erred. Its error cannot be cured by the rhetoric of the respondents.

2. As proof that Congress did not intend to treat gas transferred within a single corporate entity as a "first sale," AEPCO relied on the omission of any reference to pipeline intracorporate transactions in Section 601(b) (1) (E). That section expressly imposes the comparable price paid test on sales between an interstate pipeline and its production affiliate. Con Gas (Br., p. 12) and Mich-Wis (Br., pp. 14-15) argue that the statute *does expressly* cover pipelines engaged in production as well as pipeline production affiliates. They make the argument that the statutory term "sale *between* any interstate pipeline and any affiliate of such pipeline" (Mich-Wis Br., p. 14) is a "two-way" term, which covers both the sale *to* the pipeline by its affiliate producer and a sale *by* the pipeline [to itself] of gas it produces. But, Mid-La candidly concedes "...that

intracorporate transfers of pipeline production are *not expressly mentioned* in Section 601(b) (1) (E)...." (Emphasis added; Br., p. 28). Thus, Mid-La contradicts the other two respondents.

Respondents' effort to evade the plain and significant text of the statute by reliance on a fanciful version of the legislative history fares no better. Thus, they rely upon *allegedly relevant* legislative history comprising certain "working papers of the Conference Committee" prepared by its staff (Mich-Wis Br., pp. 15-16, App. 1A, 2A, 4A; Mid-La, Br., p. 29 and Con Gas, Br., p. 13). Only the *Reports* of the Committees and statements by the floor managers are credible as legislative history; staff working papers are not. Moreover, legislative history cannot override the unequivocal language of the statute which simply excludes gas produced by pipelines from the comparable price test of Section 601(b) (1) (E). Finally, a reading of the cited text of the working papers (Mich-Wisc, Br., App. p. 4a) shows that it does not even mention pipeline produced gas.

3. None of the respondents even attempts to rebut AEPCO's argument (Br., pp. 16-18) that Section 601(c) (2) of the NGPA, which expressly repeals the Commission's authority under NGA Sections 4 and 5, is limited to denying the pipeline the right to recover from its customers "...*any amount paid* with respect to *any purchase* of natural gas...." (Emphasis added). This expressly excludes an intracorporate transfer in which there is a mere bookkeeping entry instead of a payment and in which there is not "any amount paid" (Br., pp. 16-17). Nor does any respondent even attempt to rebut AEPCO's reliance (Br., p. 17) on *Commissioner of Internal Revenue* v. *Brown*, 380 U.S. 563, 570-571 (1965), holding that an underlined statutory term must be given its common and ordinary meaning. Respondents also fail to mention AEPCO's argument (*Id*). that the ordinary meaning of "purchase," as for example in the Uniform Commercial Code, does not encompass an intracorporate transfer.

4. None of the respondents have attempted to rebut AEPCO's argument (Br., pp. 22-25) based on prior bills

passed by Congress which would have deregulated natural gas production. Those bills show that Congress has twice, in 1950 and 1956, expressly specified its intention with respect to gas produced by a pipeline by itself or purchased from its production affiliate, and has never dealt with this issue by implication. Mich-Wis (Br., p. 24, ftn. 35) attempts to distinguish the NGPA from the earlier bills on the incredibly tenuous ground that the "unless clause" of Section 2(21) expressly makes pipeline production a first sale. Thus, Mich-Wis argues that Congress in the NGPA utilized a subsidiary clause of a definition to deregulate pipeline production as opposed to its earlier explicit language dealing with this issue of pipeline production in the very section deregulating gas!

5. None of the respondents addressed AEPCO's detailed arguments (Br., pp. 25-27) that the legislative history of the NGPA provides a strong indication that no repeal of NGPA jurisdiction over pipeline production was intended. The House version clearly intended to preserve NGA regulation of all pipeline production and the Senate intended to preserve such regulation by the Commission with respect to "old gas." Therefore, both Houses provided that regulation of "old" pipeline production under the NGA should continue. Legally, this means that the Conference Committee could have either continued NGA control over all pipeline production or deregulated *new* pipeline production only. It lacked authority to deregulate *all* pipeline production—which is exactly what the pipeline respondents claim it did. If the legislative history did (as it does not) show that this was the Conference Committee's action, it would be a legal nullity under the rules of both Houses.

6. Mid-La and Con Gas do not attempt to rebut AEPCO's argument (Br., pp. 40-41) that even if Order 58 is affirmed, the Court below unlawfully usurped the Commission's function in holding that no form of agency jurisdiction under the NGA would survive such a judicial

determination.[3] Such a holding means only that the NGPA applies to pipeline production, not that a pipeline has greater rights than a producer. The issue is whether AEPCO is correct in its view that the NGPA does not repeal or nullify the rate filing requirements of NGA Section 4 as to either pipelines or independent producers. In *Columbia Gas Development Corp.* v. *FERC,* 651 F.2d 1146, 1155-1159 (5th Cir. 1981), the Court held that a producer was not automatically entitled to collect higher NGPA ceiling prices for which it was eligible, if if did not have the contractual or statutory right to file for a rate increase. *Columbia* squarely contradicts the holding below that the NGPA impliedly repealed NGA Section 4 so that a pipeline producer was automatically entitled to NGPA prices without making a rate filing.

II. Respondents Have Made No Effective Rebuttal To AEPCO's Arguments That The Interpretation Of The Term First Sale By The Court Below Is Erroneous.

1. AEPCO argued (Br., pp. 38-39) that the Court below erred in treating Order 58 as presenting only a pure question of law, *i.e.* the interpretation of statutory language, because on its face, that Order promulgated a codified *substantive* rule. In any event, the agency was dealing with a mixed question of *policy and law* expressly committed to its discretion by Section 501(a) and 501(b) of the NGPA. No respondent has addressed this contention. Instead, they have launched elaborate defenses of the Court's standard for judicial review on the incorrect assumption that Order 58 involves only an *interpretation* of law (Mich-Wis Br., pp. 32-33; Mid-La Br., pp. 42-43).

2. AEPCO argued (Br., pp. 29-33) that the language of § 2(20) of the NGPA did not include intracorporate transfers of pipeline produced gas. Con Gas does not address this argument, or even mention this section

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[3]In its Statement of the Case (Br., p. 5, ftn. 10), Mich-Wis makes the assumption that Order 98 disappears if the Commission lacks power to deny "first sale" treatment to pipeline produced gas. This falls far short of an answer, let alone a meaningful rebuttal.

Mich-Wis (Br., p. 40) and Mid-La (Br., p. 23) argue that the disjunctive statutory definition of "sale" includes a "transfer for value" and is met by intracorporate transfers of gas. AEPCO has already answered this argument (Reply to Opp. to Cert., pp. 6-8).

3. AEPCO argued (Br., p. 36) that the interpretation below of the "unless" clause of Section 2(21) nullifies the *entire* first sale clause. No respondent has attempted to rebut this argument which exposes the blunder made by the Court below.

III. Respondents Have Not Disproved AEPCO's Thesis That The Decision Below Promotes Inequity.

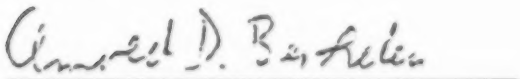
AEPCO argued (Br., pp. 27-29) that implied repeal of the Commission's powers to fix rates for pipeline production on a cost-of-service basis retroactively changed the rules of the game to the detriment of consumers. No respondent disputes the truth of our claim that cost-of-service rate regulation gave every pipeline producer the opportunity to earn its own *individual* cost-of-service. Instead, they claim that independent producers were given the same umbrella against risk that a pipeline producer operating under cost-of-service rates enjoys (Mid-La, Br., pp. 39-41 and 46-47; Con Gas, Br., pp. 24-25; Mich-Wis, Br., pp. 45-46). But, as Mid-La candidly admits (p. 40, ftn. 38), the "...significant difference was that the pipeline's cost-of-service was calculated on the basis of test-year costs and sales volumes for the individual company, whereas the area or nationwide rates were calculated on the basis of average industry-wide costs and production volumes." Thus, every pipeline enjoyed the realistic opportunity to earn a return geared to the unique circumstances of its *individual* operation while every producer had to live with *average* conditions which condemned high cost or unlucky producers to a loss. Finally, no pipeline denies AEPCO's detailed factual argument (Br., p. 15) that pipeline producers have guaranteed markets for their gas while independent producers take the risk of being unable to sell at all or unable to sell at a price which would yield a fair profit.

CONCLUSION

WHEREFORE, for the reasons set forth in AEPCO's Initial Brief and in this Reply Brief, we respectfully request that this Court find and conclude that the Court below has made an unlawful implied repeal, and grant the relief requested in the Conclusion of AEPCO's Initial Brief (Br., p. 42).

Respectfully submitted,

ARIZONA ELECTRIC
POWER COOPERATIVE,
INC.



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Reply Brief for the United States

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In the Supreme Court of the United States

OCTOBER TERM, 1982

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, PETITIONER

v.

MID-LOUISIANA GAS COMPANY, ET AL.

ARIZONA ELECTRIC POWER COOPERATIVE, INC., PETITIONER

v.

MID-LOUISIANA GAS COMPANY, ET AL.

STATE OF MICHIGAN, PETITIONER

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FEDERAL ENERGY REGULATORY COMMISSION, PETITIONER

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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

REPLY BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

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TABLE OF AUTHORITIES

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Chicago, M., St. P. & P. R.R. v. *Acme Fast Freight, Inc.*, 336 U.S. 465 8
Colorado Interstate Gas Co. v. *FPC*, 324 U.S. 581 .. 12, 13
Columbian Fuel Corp., In re, 2 F.P.C. 200 14
Energy Reserves Group, Inc. v. *Kansas Power & Light Co.*, No. 81-1370 (Jan. 24, 1983) 6, 16
Ernst & Ernst v. *Hochfelder*, 425 U.S. 185 11
FPC v. *Texaco Inc.*, 417 U.S. 380 16
Gray v. *Powell*, 314 U.S. 402 5
Howe v. *Smith*, 452 U.S. 473 15
Mastro Plastics Corp. v. *NLRB*, 350 U.S. 270 11
National Rates for Jurisdictional Sales of Natural Gas, 56 F.P.C. 509, modified in part, 56 F.P.C. 2698, aff'd *sub nom. American Public Gas Association* v. *FPC*, 567 F.2d 1016, cert. denied, 435 U.S. 907 17
Pennzoil Co. v. *FERC*, 645 F.2d 360 6
Pennzoil Co. v. *FERC*, 671 F.2d 119 6
Permian Basin Area Rate Cases, 390 U.S. 747 ..... 14, 17
Phillips Petroleum Co. v. *Wisconsin*, 347 U.S. 672 .. 4, 14
Rubin v. *United States*, 449 U.S. 424 5
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Statutes and regulation:

Natural Gas Act, 15 U.S.C. (& Supp. V) 717 *et seq.* 2
Section 1(b), 15 U.S.C. 717(b) 12
Section 2(6), 15 U.S.C. 717a(6) 15
Section 4, 15 U.S.C. 717c 12, 17
Natural Gas Policy Act of 1978, 15 U.S.C. (Supp. V) 3301 *et seq.* 2
Section 2(20), 15 U.S.C. (Supp. V) 3301(20) .. 5
Section 2(21)(B), 15 U.S.C. (Supp. V) 3301(21)(B) 2, 3, 8
Section 101(b)(9), 15 U.S.C. (Supp. V) 3311(b)(9) 6, 7
Section 105, 15 U.S.C. (Supp. V) 3315 6

Statutes and regulation—Continued Page

Section 106, 15 U.S.C. (Supp. V) 3316 6
Section 107(b), 15 U.S.C. (Supp. V) 3317(b) .. 6
Section 203(b), 15 U.S.C. (Supp. V) 3343(b) .. 9
Section 203(b)(1), 15 U.S.C. (Supp. V) 3343 (b)(1) 9
Section 203(b)(2), 15 U.S.C. (Supp. V) 3343 (b)(2) 9
Section 315(b), 15 U.S.C. (Supp. V) 3375(b) .. 6
Section 601(a)(1)(A)-(C), 15 U.S.C. (Supp. V) 3431(a)(1)(A)-(C) 15
Section 601(a)(1)(D), 15 U.S.C. (Supp. V) 3431(a)(1)(D) 15
Section 601(b)(1)(E), 15 U.S.C. (Supp. V) 3431(b)(1)(E) 7, 13
18 C.F.R. 154.42(b)(ii) 13

Miscellaneous:

123 Cong. Rec. (1977):
pp. 2141-2142 15
pp. 19964-19965 15
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p. 38362 11
pp. 38374-38375 16
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H.R. 8444, 95th Cong., 1st Sess. (1977) 10
Section 401 15
Section 416 15
H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. (1978) 10, 15
H.R. Rep. No. 95-31, 95th Cong., 1st Sess. (1977) .. 10
H.R. Rep. No. 95-496 (Pt. 4), 95th Cong., 1st Sess. (1977) 11, 14, 15
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U.S. Dep't of Energy, Energy Data Report, Domestic Natural Gas Reserves and Production Dedicated to Interstate Pipeline Companies, 1981 (1982) 4

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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

REPLY BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION

The basic assumption of the court of appeals and respondents is that Congress, in Title I of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. (Supp. V) 3301 *et seq.*, intended that there be no "distinction [with respect to first sale treatment] between pipeline and independent producers" (Pet. App. A-9) and that "pipeline producers deserve the price encouragement of NGPA no less than other producers" (*ibid.*) in furtherance of the purposes of the NGPA.

As we have demonstrated in our opening brief, the language, history, and policies underlying the NGPA do not support this thesis. Whether respondents seek to invoke the "downstream sale" theory [1] or the "intracorporate transfer" rationale, the critical fact remains that Congress in the NGPA did not disturb the Commission's traditional authority to regulate pipelines—including pipeline production—under the Natural Gas Act, 15 U.S.C. (& Supp. V) 717 *et seq.*

A. A major theme sounded by respondents (Mid-La Br. 30, 33, 36; Consol. Gas Br. 12-13, 20-21; Mich.-Wisc. Br. 10-11, 20, 25) is that Congress in the NGPA meant to treat pipeline production in precisely the same fashion as affiliate production and that, because affiliate production is granted first sale treatment under Section 2(21)(B), 15 U.S.C. (Supp. V) 3301(21)(B),[2] pipeline production is also entitled to first sale treatment.

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[1] As we developed in some detail in our initial brief (at 16-18), the "downstream sale" theory espoused by certain respondents (Consol. Gas Br. 19-20; Mich.-Wisc. Br. 38-43) is directly contrary to the statutory language and structure and was correctly rejected by the court below (Pet. App. A-8).

[2] Section 2(21)(B) provides that a statutory first sale does not occur with respect to sales by a pipeline, distributor, or

The validity of this claim is essential to respondents' case because the "intracorporate transfer" analysis, as developed by the court below (Pet. App. A-8) and heavily relied on by respondents, rests upon the assumption that the "unless" clause of Section 2(21)(B) would be rendered a "nullity" if pipeline production is not given "first sale" status. This is so, the argument runs, because pipelines do not engage in any meaningful off-system wellhead or field sales. In our opening brief (at 29 n.30), we directly challenged this assertion and demonstrated that pipelines in fact do make off-system sales that clearly qualify as "first sales" under that clause. Moreover, the fact that affiliate production is entitled to statutory "first sale" status under the Commission's interpretation while ordinary pipeline production is not, does not compel rejection of the Commission's construction of the statute.

1. To begin with, there is a clear functional difference between the activities of production affiliates and pipelines. The former make wellhead and field sales not only to their pipeline or distribution affiliates, but also to other independent purchasers.[3] On

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affiliate, "unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any *affiliate* thereof." 15 U.S.C. (Supp. V) 3301(21)(B) (emphasis added).

[3] Information submitted to the Commission by the Office of Policy Planning and Analysis of the U.S. Department of Energy and compiled by that office from the first Purchased Gas Adjustment filings made at the Commission in 1982 by the 20 major interstate pipelines referred to at Consol. Br. App. 10a n.4 shows: (1) on average, approximately one-third of the gas produced by affiliates of these 20 pipelines is sold to purchasers other than their affiliated pipelines, and (2) the production by these same affiliates is more than three

the other hand, pipeline production—except in the case of off-system wellhead or field sales—is placed in general system supply for mixed-volume sales to a pipeline's downstream system customers.

Prior to enactment of the NGPA, production affiliates, like independent producers, generally collected only area or nationwide rates for gas from their successful wells, and thus they bore the risks of production. In contrast, with respect to pipeline production priced on a cost of service basis—under which pipelines may recover all prudently incurred costs—the risks of production have been, and continue to be, borne by consumers. Thus, affiliates, unlike pipeline producers, operate for the most part exactly like independent producers.[4] And, under the Commission's interpretation of the NPGA, production affiliates are treated exactly like independent producers.

The reasonableness of treating production by affiliates differently from pipeline production is underscored by the fact that affiliate sales, like independent producer sales but unlike intracorporate transfers of pipeline production, are governed by sales contracts. Indeed, it is this requirement of a contract that com-

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times the production of their affiliated pipelines. Indeed, projected annual production in 1982 by these affiliates is about 1,690 Bcf of gas, compared to approximately 600 Bcf produced in 1981 by *all* interstate pipelines. The latter figure represents about 5.3% of all gas produced in the United States. See *U.S. Dep't of Energy, Energy Data Report, Domestic Natural Gas Reserves and Production Dedicated to Interstate Pipeline Companies, 1981*, at 2 (1982).

[4] In *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, 685 (1954), this Court recognized that regulation of sales by independent producers "is not essentially different from regulation of such sales when made by an affiliate of an interstate pipeline company."

pels the conclusion that, while Congress intended production affiliate sales to qualify as "first sales," it made a deliberate decision not to treat the "intracorporate transfer" of pipeline or distributor production in the same manner.

In Section 2(20) of the NGPA, 15 U.S.C. (Supp. V) 3301(20), Congress defined a sale as "any sale, exchange, or other transfer for value." [5] As a matter of common understanding, as well as traditional gas industry practice, an intracorporate transfer is not a sale. Nor is this requirement of contractual certainty some "hypertechnical interpretation" (Mid-La Br. 23) that the Commission invokes when it serves its purpose and rejects when it does not.[6] To the

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[5] Each of the cases cited by respondents as standing for the proposition that the language of Section 2(20) should be given a more elastic interpretation involved a form of contractual relationship. See *Rubin* v. *United States*, 449 U.S. 424 (1981) (bank loan agreement); *United States* v. *Gentile*, 530 F.2d 461 (2d Cir. 1976) (same); *United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392 (1965) (lease-sale agreement); *Gray* v. *Powell*, 314 U.S. 402 (1941) (lease of land and equipment, and operating contract).

[6] As the Commission stated in rejecting respondents' intracorporate transfer theory (Pet. App. B-65 to B-66; emphasis added):

> In its administration of the [Natural Gas Act], the Commission has not treated as a sale the transfer of pipeline produced gas into the transmission system of that pipeline. *No contracts govern that transfer*; *no certificates under the [Natural Gas Act] have been issued or were required for that transfer.* * * * We have concluded that the regulation and enforcement of rates for sales of pipeline production should not depend on an event that is recorded solely on the books and records of the pipeline and that occurs without * * * *contract*, bargaining, or certification. * * *

In our petition for certiorari (at 17-18), and in our opening brief (at 38 n.38), we explained that the method by which the

contrary, the contract limitation is a basic condition imposed by Congress in setting ceiling prices applicable to first sales generally, as evidenced by Section 101(b)(9) of the NGPA, 15 U.S.C. (Supp. V) 3311 (b)(9). See also *Energy Reserves Group, Inc.* v. *Kansas Power & Light Co.*, No. 81-1370 (Jan. 24, 1983), slip op. 4-5, 18-19 (discussing Section 105 of the NGPA, 15 U.S.C. (Supp. V) 3315).[7]

Because an intracorporate transfer of gas from the producing division of a pipeline or distributor to its transmission division is not governed by a contract, it is not subject to the realities of the marketplace. Thus, if respondents are correct that pipeline produc-

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Commission's parity pricing policy operates marks no retreat from this position, nor does it in any way support the fiction that an intracorporate transfer is a "first sale" under the NGPA.

[7] In Section 101(b)(9), Congress made it clear that in any first sale, the *contract* price controls if it is less than or equal to the applicable maximum lawful price. See also *Pennzoil Co.* v. *FERC*, 645 F.2d 360 (5th Cir. 1981). Similarly, in Sections 105 and 106 of the NGPA, 15 U.S.C. (Supp. V) 3315 and 3316—dealing with intrastate sales—the maximum lawful prices are determined by *contracts* governing those sales. Again, under Section 107(b) of the NGPA, 15 U.S.C. (Supp. V) 3317(b) (emphasis added), the Commission has the authority to establish special ceiling prices where "*necessary* to provide reasonable incentives for the production [and first sale] of * * * high-cost natural gas." The Fifth Circuit has held, in this connection, that the terms of the natural gas contract are an important element in determining the necessary incentive price. *Pennzoil Co.* v. *FERC*, 671 F.2d 119, 123 (1982). See also Section 315(b) of the NGPA, 15 U.S.C. (Supp. V) 3375(b), under which purchasers buying certain gas in a first sale are guaranteed continuing rights as to that gas, predicated solely upon expiration of the original gas purchase *contract*.

tion is entitled to first sale treatment and full NGPA pricing, pipelines would be granted greater freedom from regulation under the NGPA than either independent producers, which are subject to the contract limitation of Section 101(b)(9), or affiliates, which are subject not only to Section 101(b)(9), but also to the "affiliated entities limitation" in Section 601(b)(1)(E). See our opening brief at 37. Congress could not have intended this anomalous result.

2. Our submission that affiliate production and pipeline production are dispositively different with respect to their "first sale" status under Title I of the NGPA does not, as respondents contend (Mid-La Br. 33; Consol. Gas Br. 20-21; Mich.-Wisc. Br. 20, 25, 26, 28), disregard the close relationship between a pipeline and its production affiliate and thereby "exalt form over substance." Rather, our argument simply recognizes that in this context the two entities perform totally different roles and therefore are afforded different pricing treatment under the carefully crafted pricing framework of the NGPA.

Respondents' reliance on the "affiliated entities limitation" provision of the statute, Section 601(b)(1)(E), 15 U.S.C. (Supp. V) 3431(b)(1)(E), is equally unpersuasive. That provision limits the pass-through by interstate pipelines of the costs of gas purchased in a "first sale between any interstate pipeline and any affiliate of such pipeline" to the extent the amount paid exceeds "the amount paid in comparable first sales between persons not affiliated with such interstate pipeline." Seizing on the phrase, "first sale *between* any interstate pipeline and any affiliate of such pipeline," respondents contend (Mid-La Br. 29; Consol. Gas Br. 12; Mich.-Wisc. Br. 14-15) that a sale by a pipeline is also necessarily a first sale. But this argument begs the question, since it wholly

avoids the threshold and dispositive issue of what constitutes a "first sale." Thus, this section does not help respondents any more than does Section 2(21)(B).[8]

B. Respondents' reliance on other provisions of the NGPA and on the legislative history of the statute as

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[8] As we pointed out in our opening brief (at 23 n.25), Section 5 of the Senate bill contained an "affiliated entities limitation" provision that included pipeline production, but this reference to pipeline production was deleted in conference. Respondents urge that, notwithstanding this deletion, the conferees meant to retain the Senate approach. For this conclusion, they rely (Mid-La Br. 29 n.21; Consol. Gas Br. 13; Mich.-Wisc. Br. 15-16) on a brief memorandum dated June 6, 1978, prepared in outline form by staff counsel and distributed by Senator Jackson to the Senate conferees on the NGPA. (See Mich.-Wisc. Br. App. 2a-4a.) By its terms, however, this staff memorandum covers only "Subjects Not Addressed by the Compromise Proposal Previously Adopted." Because pipeline production is not mentioned in the memorandum, its treatment apparently had been resolved by the earlier compromise. Furthermore, it is clear that the excerpted portion of the memorandum refers only to the costs of "purchased" gas. Gas produced by pipelines is not "purchased" by the pipeline from itself; thus, "purchased" gas is a curious phrase to describe pipeline production. Moreover, the caption of the excerpted portion reads "Pass Through Of Wellhead Price Increases By Interstate Pipelines." As we pointed out in our opening brief (at 3, 29-30), pipeline production denied first sale status under the Commission's rule at issue here is not sold (or priced) at the wellhead. In addition, the portion of the staff memorandum on which respondents rely was amended by an "Errata Sheet," which explains that the purpose of the "affiliated entities limitation" provision is to ensure that the Commission does not engage in "back door" regulation of *producers*. At all events, the language of the staff memorandum, which apparently was prepared and distributed to the members of the Conference Committee without prior scrutiny by those members is entitled to little, if any, weight. Cf. *Chicago, M., St. P. & P. R.R.* v. *Acme Fast Freight, Inc.*, 336 U.S. 465, 475 (1949).

support for their intracorporate transfer theory is equally unfounded.

1. Respondents purport to rely (Mid-La Br. 20-22; Consol. Gas Br. 11-12; Mich.-Wisc. Br. 18 n.20, 24) on Section 203(b) of the NGPA, 15 U.S.C. (Supp. V) 3343(b), part of the incremental pricing provisions of the Act, to support their interpretation of "first sale." As discussed in detail in our opening brief (at 26-27), however, that provision supports our analysis, not respondents'.

In developing a method to pass through pipeline gas acquisition costs to certain industrial users, Congress defined those costs as "first sale" costs and established both a general rule of application, and a special rule limited to pipeline production. Under the general rule, the "first sale acquisition cost" depends on the "price paid * * * in any first sale." Section 203(b)(1), 15 U.S.C. (Supp. V) 3343(b)(1). As to pipelines, however, Congress provided that "the first sale acquisition cost * * * shall be *determined* in accordance with rules prescribed by the Commission." Section 203(b)(2), 15 U.S.C. (Supp. V) 3343(b)(2) (emphasis added).

Respondents assert (see, *e.g.*, Mich.-Wisc. Br. 18 n.20) that by use of this language, Congress must have assumed that there would be a Title I "first sale" price for all pipeline-produced gas. But if Congress "assumed" that pipeline production was inevitably entitled to "first sale" pricing, it surely chose odd language to achieve that end. As the Commission accurately concluded (Pet. App. B-68), this special provision "differs notably from the general rule in that it omits any reference to 'price paid' and does not indicate that such gas will be 'acquired in a first sale.'"

2. Equally unavailing are respondents' efforts to read certain language in the Conference Report as

indicative of Congress' intent that intracorporate transactions fall within the first sale definition. The relevant portion of the report states "* * * the Commission *may* define terms such as 'transfer for value' used in the definition of first sale; it *may* also establish rules applicable to intracorporate transactions under the first sale definition." H.R. Conf. Rep. No. 95-1752, 95th Cong., 2d Sess. 116 (1978) (emphasis added). Read together, these two clauses authorize the Commission to define an intracorporate transfer as a "transfer for value" (*i.e.* as a "first sale") and to "establish rules" to implement its definition. Thus, as pointed out in our opening brief (at 27-28), Congress by this language simply meant to emphasize that the Commission had the discretion to utilize its statutory authority to avoid circumvention by creating a "first sale" where the statute did not.

3. While the remaining legislative history is comparatively silent on pipeline production, what there is supports the Commission's position regarding the intent of Congress as to the scope and nature of a "first sale". See our opening brief at 22-24, 25. Respondents' attempts to show otherwise rest in large measure on selective, out-of-context excerpts from the legislative materials.

For example, respondents cite (Mid-La Br. 34 n.30; Consol. Gas Br. 15; Mich.-Wisc. Br. 23) a statement by a former Commission employee, David D. Schwartz, during the House hearings. But Mr. Schwartz's remarks produced only hostile comments and his suggestion that wellhead incentive pricing be extended to pipeline production was rejected in H.R. 8444, 95th Cong., 1st Sess. (1977), the House-passed precursor to the NGPA. See H.R. Rep. No. 95-31, 95th Cong., 1st Sess. 1 (1977). See also Brief of Public Service Commission of the State of New York (at 17-19).

Thus, this fragment from the legislative history provides no help to respondents. See *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 203-204 n.24 (1976); *Mastro Plastics Corp.* v. *NLRB*, 350 U.S. 270, 288 (1956).

Respondents take us to task (Mid-La Br. 34 n.31) for relying on a statement in the House Report, H.R. Rep. No. 95-496 (Pt. 4), 95th Cong., 1st Sess. 103 (1977). They say that the statement that first sales are "arms length" transactions has little weight because, among other reasons, first sales may include sales from a production affiliate to its parent pipeline. They do not, however, take issue with the statement in that Report that first sales are "under natural gas *contracts* * * * *for value* * * *." *Ibid.* (emphasis added).

Finally, to the extent that general, all-inclusive language was sometimes used in the debates (*e.g.*, "all gas"),[9] the answer is that it was well understood that the NGPA pricing provisions were meant to be directed at independent producers, not to the ordinary transactions of pipeline producers. See pages 13-14 & n.10, *infra*.

C. Respondents erroneously assert (Mid-La Br. 44 n.44; Mich.-Wisc. Br. 34-35) that the decision below will have no adverse impact on traditional pipeline regulation under the Natural Gas Act.

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[9] But see, *e.g.*, the statement of Congressman Dingell, Chairman of the Subcommittee on Energy and Power of the House Committee on Interstate and Foreign Commerce, and a leading advocate of the legislation in the House of Representatives, referring to the statutory price as "generally applicable to *field* sales * * *." 124 Cong. Rec. 38362 (1978) (emphasis added).

1. As discussed in our opening brief (at 22-23), the provisions in Title VI of the NGPA make clear that the NGPA was meant to have only a limited impact on the preexisting regulatory framework governing pipelines. If respondents' position is adopted, however, the delicate balance between these two regulatory schemes could be upset, with resultant disruption of both the Commission's traditional regulation over interstate pipelines under the Natural Gas Act and the states' traditional authority over intrastate pipelines and local distribution companies.

Nor are these potential concerns far-fetched. On the contrary, as a consequence of the decision below, one of the respondents herein (El Paso Natural Gas Company) has argued before the Fifth Circuit that when the Commission seeks to establish rates under Section 4 of the Natural Gas Act, 15 U.S.C. 717c, it may not exercise jurisdiction over certain pipeline production facilities by virtue of a "first sale" by the pipeline. See Motion for Order Directing Compliance with Court Mandate and for Stay of Agency Order, filed Oct. 29, 1982, in *El Paso Natural Gas Co.* v. *FERC*, No. 82-4374 (5th Cir.), at 22-23.[10] If this argument were accepted, its practical effect would be to overrule the decision in *Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945), where this Court held that Section 1(b) of the Natural Gas Act, 15 U.S.C. 717(b), "does not preclude the Commission from reflecting the production and gathering facilities of a natural gas company in the rate base and determining the expenses incident thereto for the purposes of

[10] Since the filing of the motion referred to in the text, the *El Paso* case has been transferred from the Fifth Circuit to the District of Columbia Circuit.

determining the reasonableness of rates subject to its jurisdiction." 324 U.S. at 603.

2. Respondents contend (Mid-La Br. 26-27, 36-37; Consol. Gas Br. 16-19; Mich.-Wisc. Br. 29 n.41, 33) that it is fundamentally inconsistent for the Commission to maintain, on the one hand, that the term "first sale" does not include pipeline production mixed with the pipeline's general system supply, and yet, on the other hand, to authorize interstate pipelines to value their production of certain new gas by reference to NGPA levels. This contention underscores respondents' failure to perceive the proper relationship between the Natural Gas Act and the NGPA.

In the Commission's view, Congress left to it the discretionary responsibility of "harmonizing its statutory mandate to implement the NGPA pricing scheme with its continuing authority under the [Natural Gas Act] to determine the price treatment of [pipeline system supply]" (Pet. App. B-24).[11] And it was in the course of fulfilling that responsibility that the Commission, in Order No. 98 (*id.* at B-16 to B-49), decided to continue its parity pricing policy in order to guarantee pipeline customers "a more certain stream of additional supplies" (*id.* at B-25).

3. At bottom, respondents' arguments rest on a flawed premise. They assume that, even though the basic aim of the NGPA was to address problems aris-

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[11] Thus, for example, while the Commission recognized in Order No. 98 that the absence of a contract precluded statutory first sale status to pipeline produced gas, it utilized its authority under the Natural Gas Act to impose on the valuation of pipeline produced gas given parity pricing at NGPA levels a limitation similar to, but broader than, the affiliated entities limitation in Section 601(b)(1)(E) of the NGPA (see Pet. App. B-36 to B-37). Compare 18 C.F.R. 154.42(b)(ii) with 15 U.S.C. (Supp. V) 3431(b)(1)(E).

ing from the regulation of independent producers, and even though Congress accordingly did not focus its attention on pipeline production, Congress somehow must have intended to repudiate forty years of Commission regulation of pipelines under the Natural Gas Act.

To be sure, in enacting the NGPA Congress sought to confront the distortions caused by the dual market structure and to alleviate the severe gas shortages that prevailed in the interstate market. But, as the Commission recognized, Congress sought to achieve its goals in a precise and discriminating fashion. Because regulation of independent producers and their functional equivalents had proven to be exceedingly difficult under the approach mandated by *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954), and because that approach had resulted in the dichotomy of a regulated interstate market side-by-side with unregulated state markets, Congress decided to recast the regulatory controls over those entities by overturning the *Phillips* approach while, at the same time, leaving undisturbed the longstanding method of regulating pipeline production as part of "one wholesale * * * transaction" (*In re Columbian Fuel Corp.*, 2 F.P.C. 200, 206 (1940)) under the Natural Gas Act.[12]

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[12] In *Permian Basin Area Rate Cases*, 390 U.S. 747, 756 (1968), this Court observed that, following the decision in *Phillips*, the Commission had "labored with obvious difficulty to regulate a diverse and growing industry under the terms of an ill-suited statute." The legislative history of the NGPA demonstrates that the focus of congressional concern was on the regulatory problems spawned by the decision in *Phillips*, not on any perceived problems resulting from the traditional regulation of pipeline production. See *e.g.*, S. Rep. No. 95-436, 95th Cong., 1st Sess. 7-9 (1977); H.R. Rep. No. 95-496

4. The Commission's reasoned and expert assessment of congressional intent cannot lightly be dismissed on the theory espoused by respondents (*e.g.*, Mid-La Br. 43; Mich.-Wisc. Br. 32) and adopted by the court below, *i.e.*, that the Commission had no input into the definition of "first sale." While the Commission may not have "drafted the legislation and steered it through Congress" (*Howe* v. *Smith*, 452 U.S. 473, 485 (1981)), it clearly participated meaningfully in the development and ultimate adoption of the "first sale" definition.

In May 1977, Drexel Journey, then the Commission's General Counsel, testified on the proposed legislation before the House Committee on Interstate and Foreign Commerce. See *Hearings on H.R. 6831, et al., Before the Subcomm. on Energy and Power of the*

(Pt. 4), 95th Cong., 1st Sess. 89-90 (1977); 123 Cong. Rec. 2141-2142 (1977) (remarks of Sen. McClure); *id.* at 19964-19965 (remarks of Rep. Kemp). See also H.R. 8444, Section 401 ("Findings and Purposes"), 95th Cong., 1st Sess. (1977). Indeed, the House bill included a section that would have amended the definition of "natural-gas company" in Section 2(6) of the Natural Gas Act, 15 U.S.C. 717a(6), to exclude any person making sales under certain enumerated sections of the bill. The amendment would effectively have overruled *Phillips* by excluding certain independent producer sales from Commission regulation under the Natural Gas Act. H.R. 8444, Section 416, *supra*. See H.R. Rep. No. 95-496 (Pt. 4), *supra*, at 109. The Conference Report explains that the NGPA "limits the jurisdiction of the Commission under the Natural Gas Act in a manner similar to the House-passed bill." H.R. Conf. Rep. No. 95-1752, *supra*, at 123. Accordingly, Section 601(a)(1)(D), 15 U.S.C. (Supp. V) 3431(a)(1)(D), provides that if a person's sales of certain gas are excluded from the Commission's Natural Gas Act jurisdiction by virtue of Section 601(a)(1)(A)-(C), that person shall not be included within the definition of "natural-gas company" in the Natural Gas Act.

House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess. (Pt. 2), 913-974 (1977). Indeed, in his testimony, Mr. Journey read the term "first sale" in the bill as meaning "wellhead sales." *Id.* at 967-968. Furthermore, shortly before the enactment of the NGPA, Senator Jackson sought and obtained the views of Commission Chairman Curtis on the enforceability of various provisions of the NGPA. See, *e.g.*, 124 Cong. Rec. 38374-38375 (1978); see also our opening brief at 40-42.

Beyond this, we strongly disagree with the notion that the expert views of an agency that has had many years of experience with the regulatory problems sought to be addressed in new legislation are entitled to no weight and may be disregarded simply because the agency has failed to muster sufficient evidence of its involvement in the legislative drafting process

D. Finally, respondents argue (Mid-La Br. 46-47; Consol. Gas Br. 24-25; Mich.-Wisc. Br. 45-46) that there is no unjustified windfall to the pipelines, whether the change to NGPA pricing is from the area and nationwide rates applicable to gas subject to the parity pricing policy, or from cost of service pricing.[13]

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[13] Respondents also contend that the economic impact of the lower court's decision is "minor" (Mid-La Br. 48), "a small fraction" and "*de minimis*" (Consolidated Br. 22 n.41; Mich.-Wisc. Br. 45). As we have shown in our earlier filings in this case, however, the economic impact is substantial. But even if that were not the case, respondents' legal position is nevertheless untenable. In *FPC* v. *Texaco Inc.*, 417 U.S. 380, 399 (1974), this Court observed that, "[e]ven if the effect of increased small-producer prices would make a small dent in the consumer's pocket, when compared with the rates charged by large producers, the Act makes unlawful all rates which are not just and reasonable, and does not say a little unlawfulness is permitted." See *Energy Reserves Group, Inc.* v. *Kansas Power & Light Co.*, *supra*, slip op. 10 (there is legitimate state interest in "elimination of unforeseen windfall profits").

In our initial brief (at 4-5 n.6, 33-34), we explained that area and nationwide rates were established on the basis of industry-wide cost factors. Although the last nationwide rate, for example, had a cost component for Dry Hole Expenses,[14] the producers bore the risk of incurring greater costs (including a greater frequency of unsuccessful wells) than the industry-wide average. If each well proved to be unsuccessful, the producer would recoup no costs, for no sales could be made to collect the nationwide rate. By this method, the Commission sought to "employ price functionally, as a tool to encourage discovery and production of appropriate supplies of gas." *Permian Basin Area Rate Cases*, 390 U.S. 747, 760 (1968). The incentive pricing scheme adopted in the NGPA was not a change in kind from this regulatory system.

Both the area or nationwide rate approach and the NGPA approach stand in marked contrast to the treatment of gas produced by interstate pipelines and regulated on a cost of service basis under the Natural Gas Act. Since the passage of that Act, pipelines whose production remains subject to cost of service treatment have been reimbursed by gas consumers, through rates established under Section 4 of the Act, 15 U.S.C. 717c, for *all* prudently incurred costs, including substantial lease acquisition and dry hole costs associated with the leaseholds. To be sure, these costs are determined under Section 4 of the Act on a "test year" basis. But even today, if a pipeline's pro-

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[14] See Opinion No. 770, *National Rates for Jurisdictional Sales of Natural Gas*, 56 F.P.C. 509, 540-544 (1976), modified in part, Opinion No. 770-A, 56 F.P.C. 2698 (1976), aff'd *sub nom. American Public Gas Association* v. *FPC*, 567 F.2d 1016 (D.C. Cir. 1977), cert. denied, 435 U.S. 907 (1978).

duction costs increase for certain gas, it can file for higher rates under Section 4. In short, cost of service pricing permits pipelines to recover costs for "reworking" operations, if needed to stimulate production from older wells. What cost of service pricing does not allow is the sort of windfall that would follow if NGPA prices automatically applied to this category of gas.[15]

For the foregoing reasons and those stated in our opening brief, it is respectfully submitted that the judgment of the court of appeals should be reversed.

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MARCH 1983

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[15] That production by pipelines makes up a small portion of the total gas supply underscores the point that application of the incentive pricing scheme of the NGPA to pipeline production was not necessary to alleviate the problems inherent in the dual market structure. Apart from anything else (see our opening brief at 28-29), it is inconceivable that Congress could have intended interstate pipelines to reap a windfall from an application of incentive prices that was totally unnecessary to promote the goals of the NGPA.

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Respondent's Reply Brief

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IN THE

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OCTOBER TERM, 1982

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, *et al.*,
Petitioners,

v.

MID LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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MOTION OF RESPONDENTS FOR LEAVE TO FILE REPLY AND REPLY OF RESPONDENTS TO SUPPLEMENTAL MEMORANDUM ON THE PRICING OF PIPELINE AFFILIATE GAS PRODUCTION

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MOTION OF RESPONDENTS FOR LEAVE TO FILE REPLY TO SUPPLEMENTAL MEMORANDUM ON THE PRICING OF PIPELINE AFFILIATE PRODUCTION

On April 4, 1983, this Court granted the Public Service Commission of the State of New York leave to file a supplemental brief after argument on the pricing of pipeline affiliate natural gas production. In view of certain critical errors made therein, Respondents request leave to file the attached reply.

Respectfully submitted,

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TABLE OF AUTHORITIES

CASES Page

City of Chicago v. FPC, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972) 2, 3, 4
Investigation of Pennzoil Company—United Gas Pipe Line Company Spin-Off and Related Transactions, 54 F.P.C. 2511 (1975) 4
Just and Reasonable National Rates for Sales of Natural Gas, 52 F.P.C. 1604 (1974), *aff'd sub nom. Shell Oil Co. v. FPC*, 520 F.2d 1061 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976).... 5
Just and Reasonable Rates for Sales of Natural Gas, Opinion No. 749-C, 56 F.P.C. 303 (1976).. 5
Mississippi River Fuel Corporation v. FPC, 252 F.2d 619 (D.C. Cir.), *cert. denied*, 355 U.S. 904 (1957) 2
National Rates for Jurisdictional Sales of Natural Gas, Opinion No. 770, 56 F.P.C. 509 (1976) and Opinion No. 770-A, 56 F.P.C. 2698 (1976)..... 5
Northern Natural Gas Co., 28 F.P.C. 4 (1962).... 2
Opinion No. 568, *Pipeline Production Area Rate Proceeding (Phase I)*, 42 F.P.C. 738 (1969), *aff'd sub nom. City of Chicago v. FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972) 3
Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 2
Pipeline Production Area Rate Proceeding (Phase II), 47 F.P.C. 1523 (1972) 3
Union Producing Co., 31 F.P.C. 41 (1964) 2
United Gas Pipe Line Company, 51 F.P.C. 175 (1974) 3, 4, 5

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REPLY OF RESPONDENTS TO SUPPLEMENTAL MEMORANDUM ON THE PRICING OF PIPELINE AFFILIATE GAS PRODUCTION

On March 28, 1983, the Public Service Commission of the State of New York ("New York") filed a supplemental memoradum setting forth its view on the historical pricing of natural gas produced by pipelines and pipeline affiliates. The pipeline respondents respectfully submit the following reply:

1. At the outset, three important points must be made concerning the perspective from which the issue raised by New York should be viewed. First, even if New York were correct that there was a distinction from 1972 to 1978 between the Commission's policy of pricing "old" gas produced by pipelines and "old" gas produced by pipeline affiliates, that "distinction" could not override the express language, purposes, and legislative history of the Natural Gas Policy Act ("NGPA"), all of which dem-

onstrate that Congress intended the new pricing regime to apply to all natural gas production without regard to the corporate form of the producer. Second, it is illogical to suggest, as does New York, that Congress intended to deny NGPA pricing treatment to natural gas produced by all interstate pipelines, intrastate pipelines, and distribution companies (including production which has *never* been priced on a cost-of-service basis), solely because the Commission had historically regulated a discrete vintage of interstate pipeline production on a cost-of-service basis. Finally, the historical differences between individual cost-of-service ratemaking and area or nationwide ratemaking were largely procedural, not substantive.[1] Under *both* approaches, the rates were cost-based and were designed to compensate the producer—whether pipeline, pipeline affiliate, or independent—for all reasonable costs of exploration and development, including the costs of unsuccessful ventures.[2]

2. Addressing New York's specific allegations, New York concedes that production by both pipeline and pipeline affiliates from leases acquired before October 8, 1969, was priced on a cost-of-service basis.[3] New York also concedes that production by both pipelines and pipeline affili-

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[1] This point is discussed at length in the brief of Mid Louisiana Gas Company, *et al.*, at 4-7, 39-42, and 46.

[2] *See, e.g.*, Permian Basin Area Rate Cases, 390 U.S. 747, 802 (1968), where this Court recognized that the area rates established by the Commission were based upon composite cost data consisting of "the most precise available evidence of actual historical costs."

[3] Prior to 1969 natural gas produced by an affiliate of an interstate pipeline was clearly treated for ratemaking purposes as if it were produced by the pipeline itself. *See* City of Chicago v. FPC, 458 F.2d 731, 737, n. 20 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972); Mississippi River Fuel Corporation v. FPC, 252 F.2d 619, 622 (D.C. Cir.), *cert. denied*, 355 U.S. 904 (1957); Union Producing Co., 31 F.P.C. 41, 43 (1964); Northern Natural Gas Co., 28 F.P.C. 4 (1962).

ates from any lease acquired on or after October 8, 1969, was priced at area rates in parity with independent producers for all years before the passage of the NGPA.[4] The only area of dispute concerns New York's claim as to the treatment of production from old leases during the period between the Commission's decision terminating *Pipeline Production Area Rate Proceeding (Phase II)*, 47 F.P.C. 1523 (1972), and the enactment of the NGPA on November 8, 1978. During that six-year period, the pricing of "old" pipeline and pipeline-affiliate production (*i.e.*, from leases acquired before October 8, 1969) was determined on a case-by-case basis.[5]

New York claims that from 1972 to 1978 the Commission's policy was to price so-called "old" pipeline production on a cost-of-service basis, and to price "old" pipeline-affiliate production automatically at the area or nationwide rates available to independent producers (Memorandum at 2-5). New York's claim is incorrect and unsupported. New York cites no case for this proposition. In fact, in *United Gas Pipe Line Company*, 51 F.P.C. 175 (1974), a case in which New York was an active participant, the Commission determined that no evidentiary showing had been made to permit United's pipeline affiliate, Pennzoil Producing Company, "to depart from cost-of-service pricing." *Id.* at 190. Thus, the Commission remanded the case to the administrative law judge for a determination of Pennzoil's cost-of-service. *Id.* at 191.[6]

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[4] Opinion No. 568, Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738 (1969), *aff'd sub nom.* City of Chicago v. FPC, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972). Under the Commission's regulations, however, cost-of-service pricing could be used if special circumstances were shown.

[5] The Phase II order was interpreted to require cost-of-service pricing of "old" production by both pipelines and pipeline affiliates unless it could be shown on a case-by-case basis that the public interest permitted a departure.

[6] The practical result of this order was the subsequent complete disaffiliation or severance of the pipeline and producing affiliates

In so doing, the Commission emphasized that "a 100 percent affiliate stands in the same position as does the producing arm of a pipeline company." *Id.* at 186.[7]

As noted above, New York was an active participant in the *United* proceeding. In its initial brief in that case, New York argued, contrary to the thrust of its current position, that nothing in the Commission's order of June 14, 1972, could be read as signaling a departure from cost-of-service pricing for "old" gas produced by pipeline affiliates. New York stated:

> We do not read either the Commission's order of June 14, 1972 terminating Phase II of the Pipeline Production Area Rate Proceeding or its order of August 15, 1972 granting Pennzoil Production's motion to reopen the record herein, as indicating in any manner that it intended to ignore the status of a producing entity as a division or corporate affiliate of a pipeline in determining on a case-by-case basis how the rates for its gas production from leases acquired prior to October 7, 1969 should be determined. *Nor do we see anything in these orders to indicate that the Commission intended to deviate from its consistent practice of pricing gas "sold" by such entities to the parent or affiliated pipeline on a cost-of-service basis,* unless a detailed showing had been made of how the consum-

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into two completely unrelated independent companies. The Commission approved a settlement disposing of various disaffiliation issues and the appropriate treatment of Pennzoil's production from old leases in Investigation of Pennzoil Company—United Gas Pipe Line Company Spin-Off and Related Transactions, 54 F.P.C. 2511 (1975). The approved settlement "assumes the correctness" of Opinion No. 682, where the Commission had clearly stated its policy of generally applying cost-of-service pricing to old production by pipeline and pipeline affiliates subject to review on a case-by-case basis. *Id.* at 2534 (Initial Decision).

[7] *See also* City of Chicago v. FPC, 458 F.2d 731, 737, n. 20 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972), where the court noted that affiliate production "is treated for ratemaking purposes as if it were produced by the pipeline company itself."

> ing public would benefit from a shift in pricing techniques, including a comprehensive plan of action and consumer protection of the type adopted in the Commission's subsequent order in the *Panhandle-Pan Eastern* case. . . .[8]

New York also incorrectly states that after 1972 "pipeline production from old leases continued in all cases" to be priced on a cost-of-service basis (Memorandum at 3). To the contrary, after terminating Phase II the Commission determined in Opinion No. 699-H that pipeline *and* pipeline-affiliate production from wells commenced after January 1, 1973, irrespective of when the lease was acquired, would be valued at the same nationwide rates applied to independent producers. *Just and Reasonable National Rates for Sales of Natural Gas*, 52 F.P.C. 1604, 1634-36 (1974), *aff'd sub nom. Shell Oil Co. v. FPC*, 520 F.2d 1061 (5th Cir. 1975), *cert. denied*, 426 U.S. 941 (1976).[9]

3. In summary, there was no difference in the Commission's policy on pricing pipeline and pipeline-affiliate production during the limited period 1972 to 1978; or, for that matter, during the four decades that preceded the enactment of the NGPA. Further, even if there had been a difference in treatment of pipeline and pipeline-affiliate production during that restricted period, it is illogical to suggest, as does New York, that Congress would have used that brief interlude as the reference

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[8] *See* Initial Brief of the Public Service Commission of New York in Reopened Proceeding at 4 (emphasis added), United Gas Pipe Line Co. (Pennzoil Phase I), 51 F.P.C. 175 (filed Nov. 20, 1972).

[9] Under the Commission's regulations, however, cost-of-service pricing could be used if special circumstances were shown. After 1969 in various other area and national rate orders, the Commission treated such production in an identical manner. *See, e.g.*, Just and Reasonable Rates for Sales of Natural Gas, Opinion No. 749-C, 56 F.P.C. 303, 322 (1976); National Rates for Jurisdictional Sales of Natural Gas, Opinion No. 770, 56 F.P.C. 509, 595 (1976) and Opinion No. 770-A, 56 F.P.C. 2698, 2784-86 (1976).

point for the pricing treatment of pipeline and pipeline-affiliate production rather than the far greater number of years of concededly identical treatment. In short, New York's supplemental memorandum is misleading on both a factual and a policy basis.

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Amicus Brief

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No. 81-1889, No. 81-1958,
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IN THE

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THE STATE OF MICHIGAN,
THE FEDERAL ENERGY REGULATORY COMMISSION,
Petitioners,

vs.

MID-LOUISIANA GAS COMPANY, et al.,
Respondents.

MOTION OF THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, PACIFIC GAS AND ELECTRIC COMPANY, SOUTHERN CALIFORNIA GAS COMPANY, AND SAN DIEGO GAS AND ELECTRIC COMPANY FOR LEAVE TO FILE BRIEF *AMICI CURIAE* AND BRIEF *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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MOTION OF THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA, PACIFIC GAS AND ELECTRIC COMPANY, SOUTHERN CALIFORNIA GAS COMPANY, AND SAN DIEGO GAS AND ELECTRIC COMPANY FOR LEAVE TO FILE BRIEF *AMICI CURIAE*

The Public Utilities Commission of the State of California (CPUC), Pacific Gas and Electric Company (PGandE), Southern California Gas Company (SoCalGas), and San Diego Gas and Electric Company (San Diego) respectfully move this Court, pursuant to Rule 36.2, for leave to file the accompanying amici curiae brief. This motion is necessary because all parties to the proceeding before the United States Court of Appeals for the Fifth Circuit did not consent to the filing of an amici curiae brief.

The CPUC is an administrative agency established under the Constitution and laws of the State of California. Among its duties, it exercises general regulatory jurisdiction over natural gas distribution companies within the State of California, including approval of service and rates and charges of these companies. The CPUC is obligated to protect the people of the State of California, who are customers of the gas companies, and is authorized to represent them in proceedings of this nature.

PGandE and SoCalGas are natural gas transmission and distribution companies incorporated under the laws of the State of California. PGandE distributes gas and electricity throughout the northern and central parts of California which include approximately 8.7 million people and 3.0 million gas customers. SoCalGas purchases, distributes and sells natural gas in the central and southern parts of California which include approximately 12.4 million people and 3.9 million gas customers. SoCalGas and PGandE are the largest gas distribution companies in the United States.

San Diego is incorporated under the laws of the State of California. In addition to its service of electricity, San Diego distributes gas for consumption by retail purchasers in the City of San Diego, California, and in various cities and communities in San Diego County. San Diego obtains all of its natural gas from SoCalGas.

Overall, the residential, commercial and industrial consumers within the State of California purchase more natural gas than consumers in any other state. Approximately 90 percent of the natural gas burned in California comes from sources outside the state. Over half of that supply comes from El Paso Natural Gas Company (El Paso), an interstate natural gas pipeline regulated by the Federal Energy Regulatory Commission (FERC). SoCalGas and PGandE purchase approximately 80 percent of the natural gas which El Paso transports through its interstate pipeline system. The volume of purchases by SoCalGas and PGandE make them El Paso's two largest customers.

In 1981, El Paso sold in excess of three billion cubic feet of natural gas per day to its customers or over one trillion cubic feet a year. A substantial portion of El Paso's gas supplies are the result of an extensive in-house drilling and production program, which has been ongoing for over thirty years. Approximately 80 percent of El Paso's in-house production of gas has been priced on a cost-of-service basis with the approval of the Federal Power Commission and its successor, the FERC. Thus, for over 30 years, the purchasers and consumers of El Paso's natural gas in California have, through cost-of-service pricing, paid for El Paso's risks and costs of production of said gas, plus a reasonable return on the investment in production.

The CPUC, PGandE, SoCalGas and San Diego are therefore vitally interested in the scope of the FERC's authority in the pricing of pipeline-produced gas and the outcome of this litigation. The decision of the United States Court of Appeals for the Fifth Circuit under review could permit El Paso to raise the price it charges its customers to the Natural Gas Policy Act of 1978 (NGPA) maximum lawful ceiling prices for its pipeline-produced gas. Since El Paso has no incentive to bargain with itself in an effort to keep prices at reasonable levels, El Paso can be expected to and is attempting to increase its price to the maximum lawful price, thereby increasing the price of El Paso's gas to California purchasers and consumers by hundreds of millions of dollars.

Due to the importance of the issue raised and the magnitude of the injustice created by the Court of Appeals decision, the CPUC, PGandE, SoCalGas and San Diego seek leave to file the attached brief to set forth our views on the issues presented in this proceeding, to inform this Court of the gross inequities which would result from the Court of Appeals decision and to establish that the Court of Appeals' views are inconsistent with the Congressional intent underlying the NGPA.

WHEREFORE, the CPUC, PGandE, SoCalGas and San Diego respectfully move the Court for leave to file the accompanying amici curiae brief in these proceedings.

Dated: November 17, 1982.

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TABLE OF CONTENTS

	Page
Table of Authorities	ii
Interest	2
Summary of Argument	2
Argument	3
Conclusion	8

TABLE OF AUTHORITIES

CASES — PAGE

Canadian River Gas Co., et al., 3 F.P.C. 32 (1942), *aff'd sub nom., Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945) 3

Columbia Gas Development Corp. v. *FERC*, 651 F.2d 1146 (5th Cir. 1981) 5

Democratic Cent. Com. of D.C. v. *Washington M.A.T. Com'n.*, 485 F.2d 786 (D.C. Cir. 1973), *cert. den.*, 415 U.S. 935 (1974) 6

Mid-Louisiana Gas Company v. *FERC*, 664 F.2d 530 (5th Cir. 1981) 2

Montana Power Co. v. *Federal Energy Reg. Com'n.*, 599 F.2d 295 (9th Cir. 1979) 6

Pipeline Production Area Rate Proceeding (Phase I), 42 F.P.C. 738 (1969) mod. 42 F.P.C. 1089, *aff'd sub nom., City of Chicago, Ill.* v. *FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. den.*, 405 U.S. 1074 (1972) 3-4

FERC ORDERS

Order No. 58, Docket No. RM80-7 (issued November 14, 1979) 44 Fed. Reg. 66,577 (November 20, 1979) 2, 3, 6, 7, 8

Order No. 98, Docket No. RM80-6 (issued August 4, 1980), 45 Fed. Reg. 53, 091 (August 11, 1980) 2, 6, 8

Order No. 102, Docket Nos. RM80-7 and RM80-6 (issued October 3, 1980) 45 Fed. Reg. 67,083 (October 9, 1980) 6

El Paso Natural Gas Company, Docket Nos. 69-6, et al., "Order Approving Settlement, Reserving Issue for Hearing Consolidation Dockets," 51 F.P.C. 764, rehearing denied, 52 F.P.C. 406 (1974) 4, 6

El Paso Natural Gas Company, Docket Nos. RP72-150 et al., "Order Affirming Initial Decision Adopting Settlement Proposal and Reversing Initial Decision on Rate Design Complaint," 57 F.P.C. 989 (1977) 4

STATUTES

Natural Gas Policy Act of 1978, 15 U.S.C. §3301 et. seq. 2, 5

MISCELLANEOUS

El Paso Natural Gas Company, Docket No. RP83-6-000, "Rate Change and Cancellation of Rate Schedule," 47 Fed. Reg. 47,912 (October 28, 1982) 7

124 Cong Rec. H 13115 (daily ed. October 14, 1978) (Statement of Congressman Dingell) 5

H.R. Rep. No. 95-496 (Pt. 4), 95th Cong., 1st Sess. (1977) reprinted in 1978 U.S. Code Cong. & Ad News 8454 5

H.R. Conf. Rep No. 95-1752, 95th Cong., 2d Sess. (1978) reprinted in 1978 U.S. Code Cong. & Ad News 8800 ..... 5, 6

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The Public Utilities Commission of the State of California, Pacific Gas and Electric Company, Southern California Gas Company, and San Diego Gas and Electric Company (hereinafter "California") herewith submit our brief, amici curiae, in support of petitioners, the Public Service Commission of the State of New York (No. 81-1889), Arizona Electric Power Cooperative, Inc. (No. 81-1958), the State of Michigan (No. 81-2042), and the Federal Energy Regulatory Commission

(No. 82-19). For the reasons set forth below, the United States Court of Appeals for the Fifth Circuit erred in vacating Order No. 58, 44 Fed. Reg. 66,577 (November 20, 1979), and Order No. 98, 45 Fed. Reg. 53,091 (August 11, 1980), of the Federal Energy Regulatory Commission (FERC) in the decision reported below at *Mid-Louisiana Gas Company et al.* v. *FERC*, 664 F.2d 530 (1981).

INTEREST

As set forth in the accompanying motion for leave to file brief amici curiae, which is incorporated herein by reference, California has a vital interest in the outcome of this litigation since we represent the largest group of natural gas consumers in any state in the United States. The Fifth Circuit's decision, if permitted to stand, may result in an additional increase of hundreds of millions of dollars annually in the price of natural gas to California purchasers and consumers.

Consequently, the purchasers and ultimate consumers of natural gas in California and throughout the United States will be adversely and severely affected unless this Court reverses the decision of the Court below.

SUMMARY OF ARGUMENT

The Court of Appeals' decision, disregarding the terms of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. §3301 *et seq.*, and the expertise of the FERC, will permit pipelines to unilaterally increase the prices of their own produced gas from a cost-of-service basis to higher NGPA prices. The decision ignores the intent of Congress, fundamental ratemaking principles, and equitable considerations. Purchasers and consumers of pipeline-produced cost-of-service natural gas have already substantially paid for its cost of production, and should receive the benefit of their bargain.

The Court below erred in its determination that a first sale pursuant to the NGPA occurs when a pipeline producer merely transfers from its production division to its pipeline division quantities of natural gas. In fact, no first sale takes place.

The Court's error results in defining the terms "sale" and "transfer for value" in a way that is inconsistent with the intent of Congress, the common meaning of those terms, and the long history of the regulation of pipeline production.

ARGUMENT

Prior to 1969, the Federal Power Commission (FPC), the predecessor to the FERC, priced natural gas produced by an interstate pipeline on a cost-of-service basis. *In re Canadian River Gas Co.*, 3 F.P.C. 32, 40 (1942), *aff'd sub nom. Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581 (1945). Under cost-of-service pricing a pipeline computes the amount of revenue needed to cover its lease acquisition, exploration and production costs (including dry hole costs) plus the return sought on production investment (i.e. rate base); this amount is then added to the revenue requirements for the pipeline's overall cost-of-service to be recovered through the pipeline's wholesale rates. (Order No. 98, 45 Fed. Reg. at 53,092) Pipelines could apply for rate increases to cover increased costs as often as necessary. The net effect is to shift all risks to the consumers since cost-of-service methodology permits pipeline producers to recover all prudently incurred costs, relating not only to successful drilling activities but also to "dry hole costs and other costs associated with unsuccessful and marginally successful ventures." (Order No. 98, 45 Fed. Reg. at 53,093)

In recognition of the risk-shifting effect of cost-of-service treatment and the fact that cost-of-service pricing exceeded the area rates offered to independent producers, the FPC announced in 1969 that with respect to future leases pipeline production would be priced on a parity with independently produced gas unless the pipeline justified cost-of-service treatment based on a showing of "special circumstances." *Pipeline*

Production Area Rate Proceeding (Phase I), 42 F.P.C. 738, 745 (1969), *aff'd sub nom. City of Chicago* v. *FPC*, 458 F.2d 731 (D.C. Cir. 1971), *cert. denied*, 405 U.S. 1074 (1972).[1]

On two occasions, El Paso Natural Gas Company (El Paso) availed itself of the "special circumstances" to justify cost-of-service treatment of gas. In the early 1970's, El Paso proposed and its customers agreed to the establishment of a reserve for exploration fund. The exploration project proposed by El Paso, to be conducted on leaseholds held or to be acquired by El Paso, would have been uneconomic to conduct at the then area rates established for production of natural gas. El Paso proposed that its customers provide funds for an exploration program, through the mechanism of applying refunds that would otherwise be returned to the customers. El Paso would expend the funds as required to pay immediately for 75% of any unsuccessful wells. To assure that El Paso conducted an efficient operation, it was required to pay the remaining 25% of dry hole costs. Gas produced under the program was to be priced 75% on a cost-of-service basis and 25% on an area rate basis. The customers bargained for a firm, long-term supply of gas at fixed costs (with adjustments for El Paso to account for inflation and other cost increases). In turn, El Paso received the benefit of an essentially risk-free investment at prices exceeding that of independently produced gas under area rates. The FPC approved the program. *El Paso Natural Gas Company*, 51 F.P.C. 764, *rehearing denied* 52 F.P.C. 406 (1974).

El Paso continued to find that the area rates offered by the FPC were inadequate to justify drilling wells on or after January 1, 1973, on leases acquired prior to October 8, 1969. Once again, El Paso approached its customers and offered to drill wells on those leases under a cost-of-service guarantee. Because of the long-term benefits of cost-of-service pricing, the customers again agreed, and the FPC approved the agreement. *El Paso Natural Gas Company*, 57 F.P.C. 989 (1977).

The passage of the NGPA changed the methodology for establishing prices for gas supplies by providing incentive prices

[1] At the same time, the FPC reaffirmed that gas taken in a pipeline's system from pre-1969 leases would continue to be priced on a cost-of-service basis. 42 F.P.C. at 746.

to spur development of new supplies. However, the NGPA was the result of a compromise between consuming and producing interests. While incentive prices were provided for new gas supplies, the benefits of "old" low-cost gas supplies were to be retained for consumers. *Columbia Gas Company* v. *FERC*, 651 F.2d 1146, 1160 (5th Cir.1981). The intent of Congress to balance competing interests was noted in the statements of Congressman Dingell, manager of the NGPA conference report in the House, when he stated "[t]he Natural Gas Policy Act provides reasonable price incentives, while avoiding windfall profits". 124 Cong. Rec. (Daily Ed.) Oct. 14, 1978, H 13115.

The House of Representatives recognized the inherent problems associated with giving a pipeline the power to unilaterally establish the price for its own production of gas by requiring that an arms-length transaction be an essential condition of a first sale of gas, as defined in the NGPA. According to the jurisdictional committee in the House:

> "The Committee intends that the term 'first sale' be applied by the Federal Power Commission to the first transfer of natural gas for value in an arms-length transaction. Therefore, the first sale price is essentially a wellhead price." H.R. Rep. No. 95-496 (Pt. 4), 95th Cong., 1st Sess. 103, 1977, *reprinted in* 1978, U.S. Code Cong. & Ad. News 8547.

The final conference report of the Congress retained the "first sale" definition of the House measure. H.R. Conf. Rep. No. 95-1752, 95th Cong. 2d Sess. (1978) *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983. Congress therefore intended to protect against sale prices which were not constrained by arm's-length bargaining.

Congress specifically delegated the power to implement Congress' intent with regard to intracorporate transfers of gas to the FERC. The provisions of 15 U.S.C. §3411(b) authorize the FERC to "define . . . technical and trade terms used" in the NGPA. With respect to this authority, the conference report states:

> ". . . the Commission may define terms such as 'transfer for value' used in the definition of first sale; it may also establish rules applicable to intracorporate transactions

under the first sale definition." H.R. Conf. Rep. No. 95-1752, *supra*, at 116, 1978 U.S. Code Cong. & Ad. News 9033.

FERC Order Nos. 58 and 98 represented a substantive exercise of this delegated rulemaking authority. In establishing first sale rates, the FERC considered not only the lack of arm's-length bargaining inherent in intracorporate transactions, but also who had borne the risks in obtaining pipeline production.

The FERC distinguished between gas produced through exploration and development financed by a pipeline's own money and cost-of-service gas financed by consumers. If the pipeline risked its own money, it received NGPA incentive prices. If consumers bore the financial risk of success or failure, they received gas at cost, including a reasonable rate of return to the pipeline. Under this structure, both consumers and pipelines received the benefits of their bargain.

With respect to cost-of-service gas, the FERC stated in its Order No. 102, reaffirming Orders Nos. 58 and 98, that:

> "... pipelines have already enjoyed the benefits of a certain recovery of and return on the costs of production, and that their customers, who have borne the risks of this investment in the early years of exploration and development, should have an opportunity to receive the price benefits of cost-of-service treatment for gas produced as a result of these expenditures." 45 Fed. Reg. 67,083, 67,084.

In Orders Nos. 58 and 98, the FERC attempted to maintain the most fundamental principle of ratemaking—that he who bears the financial burden of particular utility activity should also reap the benefits resulting therefrom. *Democratic Cent. Com. of D.C.* v. *Washington M.A.T. Com'n*, 485 F.2d 786, 806 (D.C. Cir. 1973), *cert. den.*, 415 U.S. 935 (1974). Indeed, the very task of regulation is to prevent consumers from bearing more than their fair share of the costs of utility service when competitive forces do not otherwise protect them. *Montana Power Co.* v. *FERC*, 599 F.2d 295, 299-300 (9th Cir. 1979).

In reversing Order No. 58, the Fifth Circuit Court of Appeals upset the delicate balance fashioned by the FERC. The decision permits inequitable windfall profits to pipelines, and leaves consumers faced with the prospect of having to pay higher prices to pipelines for gas which consumers financed and for which they assumed the risks of exploration with the expectation of reasonable cost-based prices in return. Not unexpectedly, El Paso, for example, has taken the position that it is free to reprice its own production up to the NGPA maximum lawful price. See, e.g., *El Paso Natural Gas Company*, Docket No. RP83-6-000, "Rate Change and Cancellation of Rate Schedule," 47 Fed. Reg. 47,912, 47,914 (October 28, 1982). Since El Paso has no incentive to bargain with itself to keep gas costs as low as possible, El Paso's customers are doubly injured; they have paid for the costs of El Paso's exploration programs, and they will have to pay prices for the gas that are designed to reward El Paso for undertaking the expenses and risks of exploration. Such a result is not only inequitable, but contrary to the intent of Congress.

CONCLUSION

For the above-mentioned reasons, the Court should reverse the decision of the court below, and affirm FERC Orders Nos. 58 and 98.

Dated: November 17, 1982.

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MOTION OF EDMUND G. BROWN JR., GOVERNOR OF CALIFORNIA, FOR LEAVE TO FILE A BRIEF AMICUS CURIAE AND BRIEF AMICUS CURIAE IN SUPPORT OF PETITIONERS

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Edmund G. Brown Jr., Governor of California, moves for leave to file the accompanying brief amicus curiae. This motion is necessary because a party to this proceeding refused to consent to the filing of this amicus curiae brief.

Rapidly escalating natural gas prices are already causing substantial economic problems for this state's residential, commercial, agricultural and industrial consumers. Residential consumers of natural gas in Southern California are expected to pay 70% more for this fuel this winter than last. Major industrial consumers are already switching from clean burning natural gas to fuel oil because of the rising price of gas. If substantial fuel switching occurs, literally tons of increased pollutants will be discharged into the air. This will have a direct and immediate effect on the health and safety of large numbers of California's citizens. All regions of the state are seriously affected by precipitously increasing natural gas costs.

Further price increases can only worsen these already critical problems. Unless overturned by this Court, the decision below will result in significantly increased natural gas costs for California consumers, and deterioration in the economic and physical health of the citizens of this state. For these reasons, the Governor has a vital interest in the outcome of this case.

The Governor is aware that an amici curiae brief will be filed at this stage of the proceeding by the California Public Utilities Commission in conjunction with major California utilities. The Governor does not wish to displace or diminish the role of these amici. However, because of the diverse and serious problems which will be created by an adverse decision in this case, the Governor's interest is substantially broader than that of the California Public Utilities Commission and associated utility companies.

The Governor is California's "official organ of communications" with the federal government. Cal. Gov. Code §12012. In this role and as the chief executive of one of the largest natural gas consuming states in the nation, the Governor closely monitored the legislative deliberations which led to enactment of the Natural Gas Policy Act of 1978 (NGPA). As a consequence, the Governor brings to this proceeding an intimate knowledge of the legislative history of the NGPA. Indeed, the Governor is aware of elements of the legislative history of the NGPA which are essential to an informed judgement in this case.

Because of the Governor's acute interest in this case and his ability to provide insight into the legislative history of the NGPA, the Governor of California seeks leave to file the attached amicus curiae brief in support of petitioners.

November 17, 1982.

Respectfully submitted,

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TABLE OF CONTENTS

Page

Table of Authorities iii

Opinion Below 2

Statutes Involved 2–3

Interest 3–4

Summary of Argument 4–6

Argument 6

I

The decision below is not supported by the legislative history of the Natural Gas Policy Act 6

II

The implementation of the "first sale" definition by the Federal Energy Regulatory Commission merits deference in this case 13

Conclusion 19

TABLE OF AUTHORITIES

Cases

Page

Adams v. United States, 319 US 312 (1943) 16
Batterton v. Francis, 432 US 416 (1977) 18
Ford Motor Credit Co. v. Millhollen, 444 US 555 (1980) 16
New York State Dept. of Social Services v. Dublino, 413 US 405 (1973) 16
Norwegian Nitrogen Products Co. v. United States, 288 US 294 (1933) 18
Tenneco Oil Co. v. Federal Energy Administration, 613 F. 2d 298 (TECA, 1979) 11
Udall v. Tallman, 380 US *reh. den.* 380 US 989 (1965) 18
United States v. Johnston 124 US 236 (1888) 17
United States v. Moore, 95 US 760 (1878) 16

FERC Rules and Orders

Interim Regulations, Natural Gas Policy Act of 1978, 43 Fed. Reg. 56448 (December 1, 1978) 14, 16
Order No. 58, Docket No. RM 80-7 (November 14, 1979) 14
Order No. 98, Docket No. RM 80-6 (August 4, 1980) 14
Order No. 102, Docket Nos. RM 80-6 and RM 80-7 (October 3, 1980) 14

Statutes

Natural Gas Policy Act of 1978, 15 USC (Supp.IV) § 3301 *et seq.* passim
Section 2(20), 15 USC (Supp.IV) § 3301(20) 13
Section 2(21), 15 USC (Supp.IV) § 3301(21) 4, 13
Department of Energy Organization Act, PL 95-91, 42 USC 7171 *et seq.* 14

Miscellaneous

H.R. Rep. No. 95-496 (Pt. 4), 95th Cong., 1st Sess. *reprinted in* 1978 U.S. Code Cong. & Ad. News 8454 ..... 4, 9
H.R. 5289, as amended, 123 Cong.Rec. 32306–32307 (1977) 5, 11
H.R. Doc. 95-128, 95th Cong., 1st Sess. (Address by the President of the United States, April 20, 1977) 6–7
Excerpt from "The National Energy Plan", Executive Office of the President, April 29, 1977, S.Rep. No. 95-436, 95th Cong., 1st Sess. *reprinted in* 1978 U.S. Code Cong. & Ad. News 7865 7
H.R. Doc. 95-138, 95th Cong., 1st Sess. (National Energy Act, Communication from the President of the United States) 7–8
Hearings on the National Energy Act, Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess. *(Comm. Print 95-23, 1977)* 8

Page

H.R. Rep. No. 95-543, 95th Cong., 1st Sess. (1977) *reprinted in* 1978 U.S. Code Cong. & Ad. News 7673 ..... 8, 9

H.R. Rep. No. 95-543, Vol. II Appendix, 95th Cong., 1st Sess. (1977) 9–10

123 Cong. Rec. 32206 (1977) (Statement of Senator Pearson) 10

123 Cong. Rec. 32306 (1977) (Senate vote on Pearson-Bentsen amendment) 5, 11

S.Rep. No. 95-436, 95th Cong., 1st Sess. 36 (1977) *reprinted in* 1978 U.S. Code Cong. & Ad. News 7883 11

Staff of Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess., *Economic Analysis of Natural Gas Policy Alternatives* (Comm. Print 95-31, 1977) 11

S. Conf. Rep. No. 95-1126, 95th Cong., 2nd Sess. (1978) 11

Staff of Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 2nd Sess., *Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978* (Comm. Print 95-62, 1978) 12

H.R. Conf.Rep. No. 95-1752, 95th Cong., 2nd Sess. *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983 ..... 12, 13

Department of Energy FY 1979 Authorization, Hearings before the Subcomm on Energy Conservation and Regulation of the Senate Comm on Energy and Natural Resources, 95th Cong., 2nd Sess. (Pub. No. 95-174, 1978) 15

124 Cong.Rec. 38345–38358 (1978) (Hollis memorandum) 15

124 Cong.Rec. 38374-38375 (1978) (Curtis letter) 16

Department of Energy FY 1980–81 Authorization, Hearings on S.688 Before the Subcomm. on Energy Regulation of the Comm. on Energy and Natural Resources, 96th Cong., 1st Sess. (Pub. No. 96-27, 1979) 17

No. 81-1689, No. 81-1958, No. 81-2042, No. 82-19

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1982

THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
THE STATE OF MICHIGAN,
THE FEDERAL ENERGY REGULATORY COMMISSION,
Petitioners,

vs.

MID-LOUISIANA GAS COMPANY, ET AL.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF AMICUS CURIAE OF EDMUND G. BROWN JR., GOVERNOR OF CALIFORNIA, IN SUPPORT OF PETITIONERS

Edmund G. Brown Jr., Governor of California, herewith submits his brief amicus curiae in support of petitioners Public Service Commission of the State of New

York (No. 81-1889), Arizona Electric Power Cooperative, Inc. (No. 81-1958), the State of Michigan (No. 81-2042), and the Federal Energy Regulatory Commission (No. 82-19). For the reasons set forth below, the United States Court of Appeals for the Fifth Circuit erred in vacating Orders Nos. 58 and 98 of the Federal Energy Regulatory Commission in the decision reported as *Mid-Louisiana Gas Company, et al.* v. *Federal Energy Regulatory Commission*, 664 F.2d 530 (1981).

OPINION BELOW

The opinion of the court of appeals (Pet.App. A-1 to A-15) [1] is reported at 664 F.2d 530. The orders of the Federal Energy Regulatory Commission (Pet.App. B-1 to B-13, B-14 to B-49 and B-50 to B-82) are not reported.

STATUTES INVOLVED

1. Section 2(20) of the Natural Gas Policy Act of 1978, 15 U.S.C. (Supp. IV) 3301(20), provides:

> The term "sale" means any sale, exchange, or other transfer for value.

2. Section 2(21) of the Natural Gas Policy Act of 1978, 15 U.S.C. (Supp. IV) 3301(21), provides:

> (A) General rule
>
> The term "first sale" means any sale of any volume of natural gas—
>
> (i) to any interstate pipeline or intrastate pipeline;
>
> (ii) to any local distribution company;

[1] "Pet.App." refers to the appendix to the petition in No. 81-1889.

(iii) to any person for use by such person;
(iv) which precedes any sale described in clauses (i), (ii), or (iii); and
(v) which precedes or follows any sale described in clauses (i), (ii), (iii), or (iv) and is defined by the Commission as a first sale in order to prevent circumvention of any maximum lawful price established under this chapter.

(B) Certain sales not included

Clauses (i), (ii), (iii), or (iv) of subparagraph (A) shall not include the sale of any volume of natural gas by any interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof, unless such sale is attributable to volumes of natural gas produced by such interstate pipeline, intrastate pipeline, or local distribution company, or any affiliate thereof.

INTEREST

As set forth in the accompanying motion for leave to file a brief amicus curiae, which is herein incorporated by reference, the Governor of California has a vital interest in the outcome of this litigation. Current natural gas prices are already hurting every segment of California's gas-intensive economy. Residential consumers in Southern California in particular will soon see their bills almost double for natural gas. Industrial consumers are already beginning to switch to fuel oil because of the costs of vital natural gas. Further switching will lead to degradation of California's air quality and represent a very real threat to the health of California's citizens.

If the decision below is permitted to stand, California consumers will face yet higher gas prices. This can only exacerbate these already critical problems.

For these reasons, the Governor of California is acutely interested in this case.

SUMMARY OF ARGUMENT

In his previous brief in support of petitions for a writ of certiorari to the Fifth Circuit Court of Appeals, the Governor of California made a series of arguments against the reinterpretation by the court below of the critical "first sale" definition in the Natural Gas Policy Act (NGPA). 15 USC (Supp.IV) § 3301 (21). In the interest of brevity, the Governor does not repeat these arguments in this brief but would recall them to the Court's attention and make the following additional points.

First, the court below was unaware of critical elements of the legislative history of the NGPA. This led, among other missteps, to the lower court's opinion that the rules and orders of the Federal Energy Regulatory Commission (FERC) implementing the first sale policy of the NGPA affront "(t)wo of the overriding purposes of the NGPA . . . to eliminate the dual interstate and intrastate market for natural gas and to provide higher prices to encourage production." Pet.App. A-9. Apparently unknown to the court below is the fact that two House committees and the House of Representatives itself found no inconsistency between these selfsame policies and the limitation of first sale status to "arms-length transactions". H.R. Rep. No. 95-496 (Pt.4), 95th

Cong., 1st Sess. 103 (1977) *reprinted in* 1978 U.S. Code Cong. & Ad. News 8547. This standard would undeniably preclude "first sale" status for the accounting transfers granted first sale status, and related incentive prices, by the court below. Recognizably, the lower court stands apart from the legislative history of the NGPA in finding a fundamental conflict between these policies and a limitation of automatic "first sale" status to actual sales of natural gas.

Also unknown by the lower court was that the Senate bill sent to conference would have granted high incentive prices to accounting transfers of gas. The Senate bill achieved this by granting incentive price treatment to gas "sold *or delivered* in interstate commerce". HR 5289, as amended, 95th Cong., 1st Sess., 123 Cong.Rec. 32306 (1977) (emphasis added). Notably absent from the conference report and the text of the "first sale" definition is the "or delivered" formulation of the Senate. The only reasoned conclusion is that the Committee of Conference implicitly rejected automatic "first sale" status for accounting transfers of gas.

Second, the lower court completely discounted the implementation of the NGPA's "first sale" definition by FERC. The Governor submits that this is a mistake. FERC's implementation of the "first sale" definition merits deference in this case.

FERC's rules and orders lead to a fundamentally fair result. By these FERC actions, both downstream consumers and pipeline companies get the benefits of their bargains. Pipeline companies receive high NGPA prices

for gas for which they paid the costs of exploration and development; consumers are protected from a double dip into their pocketbooks for "cost-of-service" gas.

The public record supports the view that FERC personnel contemporaneously interpreting the NGPA were intimately aware of the intent of Congress in enacting the NGPA. Based on this record, it is inconceivable that FERC was so isolated from the legislative process that it grossly misapplied the critical "first sale" definition.

FERC's implementation of the "first sale" definition represents a judgment call, one of many made by an agency completing the "enormously difficult job" of implementing a complex new law. In light of the paucity of support for the lower court's second-guessing of FERC, this Court should have no hesitation in reversing the decision of the court below.

I

THE DECISION BELOW IS NOT SUPPORTED BY THE LEGISLATIVE HISTORY OF THE NATURAL GAS POLICY ACT

The Natural Gas Policy Act (NGPA) represents a balance between producer and consumer interests, largely reflected as compromises between the Senate and the House, supported by the President. By ignoring this fact, the court below reached a conclusion contrary to the letter and intent of the Act.

What was to become the NGPA started as one element of President Carter's proposal for a comprehensive energy strategy for the nation. *See* H.R. Doc. 95-128, 95th Cong., 1st Session (address by the President of the

United States, April 20, 1977). The natural gas portion of the President's energy plan was premised on the conclusion that "Government Policy should provide for prices that encourage development of new fields and a more rational pattern of distribution; *but should also prevent windfall profits*". Excerpt from "The National Energy Plan, Executive Office of the President, April 29, 1977, S.Rep. No. 95-436, 95th Cong., 1st Session, *reprinted in* 1978 U.S. Code Cong. & Ad. News 7865 (emphasis added).

This triad of policies was reflected in various ways in the President's proposed reforms of the nation's natural gas laws. *Id.* To address severe market distortions created by the existence of unregulated intrastate markets and interstate markets subject to cost-based regulation under the Natural Gas Act, the President proposed to extend federal control to previously unregulated intrastate production. A new commodity-based pricing system was to be established which would hike prices for a defined category of new gas production to equivalence with oil. Even higher prices were to be authorized for very high cost categories of gas production. To cushion the shock of these substantially higher new gas prices to consumers, these price increases were to be allocated first to industrial consumers of gas, a so-called incremental pricing provision. It is in the draft of legislation to implement these initiatives sent to the Congress by the President that a "first sale" appears as an undefined condition precedent to receipt of incentive new gas prices. H.R. Doc. 95-138, 95th Cong., 1st Sess. (National

Energy Act, Communication from the President of the United States) 56–60.

In the House, the President's proposal was refined, but left largely intact. In hearings before the Subcommittee on Energy and Power of the House Committee on Interstate and Foreign Commerce, expert witnesses expressed confusion about the meaning and operative effect of the key "first sale" term. *Hearings on the National Energy Act Before the Subcomm. on Energy & Power of the House Comm. on Interstate and Foreign Commerce,* 95th Cong., 1st Session (Comm. Print 95-23, 1977) 967–968. That confusion was eliminated with the definition of this term in the Committee's report. The Committee stated:

> The Committee intends that the term "first sale" be applied by the Federal Power Commission to the first transfer of gas for value *in an arms-length transaction.* Therefore, the first sale price is essentially a wellhead price. H.R. Rep. No. 95-496 (Pt.4), 95th Cong., 1st Sess. at 103 (1977) *reprinted in* 1978 U.S. Code Cong. & Ad. News 8547. (Emphasis added)

Recognizably, this definition would deny "first sale" status to transfers of gas from an interstate pipeline company's wells to its pipeline because such transfers are simply not "arms-length transactions".

The court below suggests that such a result would affront "(t)wo of the overriding purposes of the NGPA . . . to eliminate the dual interstate and intrastate market for natural gas and to provide higher prices to encourage production." Pet.App. A-9. However, within two pages of the House Commerce Committee's "first

sale" definition, the report states that the purposes of its reported bill include the elimination of ". . . the distortions created by the simultaneous existence of a regulated interstate market and an unregulated interstate market" and the provisions of "positive price incentives to encourage expanded exploration . . ." H.R. Rep. No. 95-496 (Pt.4), 95th Cong., 1st Sess. (1977) 101 *reprinted in* 1978 U.S. Code Cong. & Ad. News 8545. It is unmistakable that the court below stands apart from the jurisdictional committee of the House in finding a conflict between these policies and a limitation of automatic "first sale" status to arms-length transactions, or actual sales.

The bill was next considered in the House by the Ad Hoc Energy Committee, a special committee created to reconcile the elements of the President's omnibus energy proposal adopted by various standing House committees. H.R. Rep. No. 95-543, 95th Cong., 1st Sess. (1977) 3 *reprinted in* 1978 U.S. Code Cong. & Ad. News 7673. After changes in the definition of new natural gas in the Commerce Committee reported bill, *Id.* at 40–47, 1978 U.S. Code Cong. & Ad. News 7707–7714, the Ad Hoc Committee reported this measure to the floor. No change was made in the Commerce Committee's "first sale" definition. Rather, the Ad Hoc Committee report states that "all of the legislative history developed by the standing committees . . . attaches . . ." to the bill sent to the House floor. *Id.* at 3, 1978 U.S. Code Cong. & Ad News 7673. The report of the House Interstate and Foreign Commerce Committee was reprinted with the Ad

Hoc Committee report. H.R. Rep. No. 95-543, Vol. II Appendix, 95th Cong., 1st Sess. (1977).

Like the House Commerce Committee, the Ad Hoc Committee, which included the later House conferees on the NGPA, found no inconsistency between the goals of a single national market for gas, increased incentive prices, and limitation of "first sale" status to "arms-length transactions". The bill reported by the Ad Hoc Energy Committee was passed by the House on October 13, 1977.

In the Senate, a vastly different policy was developed. Despite arguments of opponents of deregulation that "Senate action is really irrelevant since President Carter and House Speaker O'Neill are opposed to deregulation", 123 Cong. Rec. 32206 (1977) (Statement of Senator Pearson), the Senate passed a bill containing the Pearson-Bentsen amendment which would have rapidly deregulated gas to be sold in the interstate market. 123 Cong. Rec. 32306–32307 (1977). While the President's proposal would make deregulation possible by 1985, S.Rep. No. 95-436, 95th Cong., 1st Sess. (1977) 36 *reprinted in* 1978 U.S. Code Cong. & Ad. News 7883, the Administration bill, in contrast to the Senate measure, met the recognized problems of the then current system "with far less risk of exorbitant near-term price increases and excessive producer windfall profits." *Id.* at 34, 1978 U.S. Code Cong. & Ad. News 7882.

House analysts made the same point. Compared to the targeted incentives approach of the House and Administration, the Senate's broad brush granting of price incen-

tives would result in a "small increase in conventional natural gas production . . . (which) . . . would cost the nation's consumers more than $24 per Mcf and would be equivalent to paying $140 per barrel of oil." Staff of Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 1st Sess., *Economic Analysis of Natural Gas Policy Alternatives* (Comm. Print 95-31, 1977) 9.

Among other differences between the House and Senate bills, the Senate-passed measure contained no "first sale" or other similar limitation. Rather, the Senate-passed bill deregulated new natural gas "sold *or delivered* in interstate commerce" after a certain date. H.R. 5289, as amended, 95th Cong., 1st Sess. 123 Cong. Rec. 32306 (1977) (emphasis added). The "or delivered" language of the bill would have encompassed the kinds of accounting transfers of gas granted "first sale" status by the court below since no actual sale as that term is generally used would be required. *Tenneco Oil Co.* v. *Federal Energy Administration,* 613 F.2d 298 (TECA, 1979).

In conference, the polar approaches of the House and Senate were resolved. The conference pitted the House and Administration against nine Senate conferees, five of whom had voted against the Pearson-Bentsen amendment on the floor of the Senate.[2]

The result was a compromise along the lines of the House bill which sought "to minimize the consumer

[2] *Compare* votes on the Pearson-Bentsen amendment, 123 Cong. Rec. 32306 (1977) with Senate signatories to the conference report, S.Conf.Rep. No. 95-1126, 95th Cong., 2nd Sess. 125.

costs of natural gas pricing policies" as well as an attempt "to focus producer incentives onto those categories of natural gas where increased discovery and production appear feasible." Staff of the Subcomm. on Energy and Power, House Comm. on Interstate and Foreign Commerce, 95th Cong., 2nd Sess., *Economic Analysis of H.R. 5289, Natural Gas Policy Act of 1978* (Comm. Print No. 95-62, 1978) 8.

When compared to the House bill, the conference agreement reflects a policy of specifying what was left implicit in the House bill. *See generally* H.R. Conf.Rep. No. 95-1752, 95th Cong., 2nd Sess. 67–69 *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983–8985. Specific statutory ceiling prices and expedited deregulation of high cost gas production categories are established. Consistent with Administration analyses that deregulation would be possible by 1985, most categories of new gas production are freed from federal price controls on January 1, 1985, subject to Presidential or Congressional reimposition of controls if necessary. An incremental pricing provision preserving the essence of the House policy was included.

With respect to the tying of the receipt of incentive prices to a "first sale" of gas, the House prevailed as it had on other important matters. The conference report tells the story:

> The price ceilings provided by the Conference agreement apply to the "first sale" of any natural gas. The first sale, which is defined in Sec. 2, means any *sale* of any volume of natural gas to any pipeline, to any local distribution company, to any person for his

> use, and all *sales* occurring before such sales. H.R. Conf.Rep. No. 95-1752, 95th Cong., 2nd Sess. 74–75 *reprinted in* 1978 U.S. Code Cong. & Ad. News 8991 (emphasis added).

Notably absent from this explanatory statement and the Act's "first sale" definition, 15 USC (Supp IV) §§ 3301 (20) & 3301 (21), is the "or delivered" formulation of the Senate. The only reasoned conclusion to be drawn from this significant omission is that in choosing between the clear options presented by the House and Senate bills, the Committee of Conference chose the more tailored House approach.

The court below would engraft onto the NGPA a policy included in the Senate bill but rejected by the Committee of Conference. This policy of granting high incentive prices to gas merely "delivered in interstate commerce" may or may not make good sense. However, this policy was specifically rejected by the Congress when it embraced the "first sale" requirement of the House bill. To change this policy is the prerogative of Congress, not the prerogative of the Fifth Circuit Court of Appeals.

II

THE IMPLEMENTATION OF THE "FIRST SALE" DEFINITION BY THE FEDERAL ENERGY REGULATORY COMMISSION MERITS DEFERENCE IN THIS CASE

The Federal Energy Regulatory Commission's actions concerning the "first sale" definition merit support by this Court for three major reasons. First, FERC's rules

and orders lead to a fundamentally fair result. Interim Regulations, Natural Gas Policy Act of 1978, 43 Fed.Reg. 56448 (December 1, 1978), Order No. 58, Docket No. RM 80-7 (November 14, 1979), Order No. 98, Docket No. RM 80-6, Order No. 102, Docket No. RM 80-6 and RM 80-7 (October 3, 1980). Pipeline production is granted NGPA incentive prices if the pipeline and its shareholders bore the risks of finding and developing new gas supplies. If downstream customers bore the financial risks of exploration and development, they receive that gas at cost plus a reasonable rate of return to the pipeline. Conversely, if this Court embraces the interpretation of the court below, downstream customers will pay twice for "cost-of-service" gas, the "double dip into consumers' pocketbooks" described in the Governor's previous brief at pages 9–15. This would be manifestly unfair and contrary to the intent of Congress. *Id.*

Second, against the background of FERC's involvement in the development of the NGPA, it is almost inconceivable that FERC did not understand the intentions of Congress with respect to the threshold "first sale" term. The court below readily dismisses FERC's implementation of the "first sale" definition because the agency "had no input into the development of the term 'first sale' ". Pet.App. A-7. This is literally true. FERC did not exist at the time the President's draft bill was submitted to the Congress nor when the House Commerce Committee defined this term in its report.[3]

[3] The President's draft was submitted to Congress on April 29, 1977. H.R. Doc. No. 95-183, 95th Cong., 1st Sess. (1977). The House Commerce Committee report is dated July 19, 1977. H.R. Rep.

However, this does not mean that FERC was so estranged from the development of the NGPA that its expert opinion should be so discounted by the court below. Indeed, the public record supports the view that this is a case in which agency personnel contemporaneously interpreting the NGPA, while perhaps not actually the draftsmen of the Act, were deeply familiar with its development and meaning. The Chairman of FERC, Charles B. Curtis, was in close touch with members of the conference committee.[1] Other FERC staff were also involved. A memorandum critical of the administrative feasibility of an early draft of the conference agreement prepared by Sheila S. Hollis, Director of FERC's Office of Enforcement, played an important role in the debates on the NGPA. 124 Cong. Rec. 38345–38358 (1978). A

No. 95-496 (IV *reprinted in* 1978 U.S. Code Cong. & Ad. News 8454. FERC came into being on Aug. 4, 1977. D.O.E. Organization Act, PL 95-91, 42 USC § 7171 *et seq.*

[1] This became a major issue in Senate oversight hearings. *Dept. of Energy FY 1979 Authorization, Hearings before the Subcomm. on Energy Conservation and Regulation of the Senate Comm. on Energy and Natural Resources,* 95th Cong., 2nd Sess., (Pub. No. 95-174, 1978) 665–727. Chairman Curtis was invited to and attended meetings among conferees on the NGPA "to lend assistance to be available to respond to questions on the Natural Gas Act and proposed changes that were under consideration by some Members of the House and some Members of the Senate." *Id*. at 667. He had conversations with numerous Members of the House and Senate during the conference deliberations on the NGPA. *Id*. at 708–709. This level of involvement by FERC's then chairman derived from the relationships and reputation for integrity and expertise he had developed as a member of the professional staff of the Committee on Interstate and Foreign Commerce, the jurisdictional committee in the House of Representatives. *Id*. at 720. This legislative history does not support the inference that FERC was frozen out of the development of the NGPA.

subsequent letter from FERC's chairman indicates that virtually all of the problems identified in the Hollis memorandum were corrected in the final conference draft of the NGPA. 124 Cong. Rec. 38374–38375 (1978).

Within weeks after the President signed the NGPA into law, FERC issued its first rules implementing, among other matters, the key "first sale" definition of the Act. Interim Regulations, Natural Gas Policy Act of 1978, 43 Fed.Reg. 56448 (December 1, 1978). In those rules, FERC concluded that the results associated with a reinterpretation of the NGPA endorsed by the court below "were clearly not intended by the legislative draftsman". *Id.* at 56463. To suggest, as does the court below, that this was not based on an intimate knowledge of the letter and spirit of the NGPA would require this court to ignore the obvious and continuing involvement of FERC personnel in developing the NGPA. Rather, it appears that FERC knew very well what was intended by the Congress and implemented the letter of the Act in its rules and orders.

It is submitted that his court should not depart from its long standing practice of giving great deference to the interpretation of a statute by those required to administer it. *United States v. Moore,* 95 US 760 (1878), *New York State Dept. of Social Services v. Dublino* 413 US 405 (1973). This is particularly appropriate where, as here, the agency was directly involved in the development of the legislation being interpreted. *Adams v. United States,* 319 US 312 (1943), *Ford Motor Credit Co. v. Millhollen,* 444 US 555 (1980).

Third, FERC's implementation of the "first sale" policy of the NGPA represents a judgment call of an expert federal regulatory agency. The making of such judgment calls is the very reason for the existence of administrative agencies. There were many judgment calls in the implementation of this extremely complex new act. This was recognized by the Congress. But even an early critic of the President's program, Senator J. Bennett Johnston of Louisiana, Chairman of the Subcommittee on Energy Regulation of the Senate Committee on Energy and Natural Resources, was moved to tell FERC's chairman after implementation of the NGPA was well under way:

> The truth of the matter is you have an enormously difficult job. You really do, and the Congress wrote the act, and you have to administer it, and I don't always agree with what you have done, certainly on the most favored nation clauses, although that was partially fixed. But aside from that, I think you have done a fine job of a very difficult task, . . . *Department of Energy FY 1980–81 Authorization, Hearings on S.688 Before the Subcomm. on Energy Regulation of the Senate Comm. on Energy and Natural Resources,* 96th Cong., 1st Sess., (Pub.No. 96-27 1979) 20 (Statement of Senator Johnston).

It is in pragmatic deference to such difficult tasks of implementation that this Court has recognized that contemporaneous construction of a new statute by those charged with its administration should not be overturned except for weighty reasons. *United States v. Johnston,* 124 US 236 (1888), *Norwegian Nitrogen*

Products Co. v. United States, 288 U.S. 294 (1933), *Udall v. Tallman,* 380 US 1 *reh. den.* 380 US 989 (1965). Where, as here, the plain meaning and legislative history of the "first sale" definition do not reveal that FERC's implementation of the first sale policy of the NGPA was "arbitrary, capricious, an abuse of discretion or otherwise not in accordance with law", *Batterton* v. *Francis,* 432 U.S. 416, 420 (1976), this Court should have no hesitation in supporting FERC's implementation of the NGPA's "first sale" definition.

CONCLUSION

For the reasons set forth above, the decision of the Court of Appeals for the Fifth Circuit should be reversed.

Dated: November 17, 1982.

Respectfully submitted,

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Nos. 81-1889, 81-1958, 81-2042, 82-19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
STATE OF MICHIGAN,
FEDERAL ENERGY REGULATORY COMMISSION,
Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF AMICUS CURIAE OF PUBLIC POWER GROUP IN SUPPORT OF PETITIONERS

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City of Stillwater, Utilities Authority

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TABLE OF CONTENTS

	Page
Interest of Amicus Curiae	2
Summary of Argument	3
Argument	4
Background	4
I. The Court of Appeals Erred in Holding That NGPA Impliedly Repealed Commission Jurisdiction Over Pipeline Production	6
II. The Result Reached by the Court Below Conflicts With National Energy Policy	10
Conclusion	15

TABLE OF AUTHORITIES

Cases:

City of Chicago v. F.P.C., 458 F.2d 731 (D.C. Cir. 1971), cert. denied, 405 U.S. 1074 5
City of Detroit v. F.P.C., 230 F.2d 810 (D.C. Cir. 1955), cert. denied, 352 U.S. 829 4
Consumer Energy Council v. F.E.R.C., 673 F.2d 425 (D.C. Cir. 1982) 5, 11
Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 5
Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672 (1954) 5, 6, 8
Pipeline Production Area Rate Proceeding, 42 FPC 738 (1969) 5, 8

Statutes:

Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. § 717 *et seq.* 2, 4, 5, 6
Natural Gas Policy Act, 92 Stat. 3351, 15 U.S.C. § 3301 *et seq.* (Supp. IV 1980) ..... *passim*
Section 2, 15 U.S.C. § 3301 ..... 7, 8, 10, 13
Sections 101-110, 15 U.S.C. §§ 3311-3320 ..... 6, 10
Section 203, 15 U.S.C. § 3343 10
Section 501, 15 U.S.C. § 3411 12

Page

Omnibus Budget Reconciliation Act of 1981, P.L. 97-35, 95 Stat. 614 14
Powerplant and Industrial Fuel Use Act, P.L. 95-620, 92 Stat. 3289 ..... 13, 14

Miscellaneous:

DOE, Economic Regulatory Administration, Public Interest Exemption Option Analysis (Feb. 21, 1980) 13
DOE, Economic Regulatory Administration, Order Granting Exemptions (Mar. 4, 1980) 13
H.R. Rep. No. 97-158, 97th Cong., 1st Sess., Vol. II 14

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ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
STATE OF MICHIGAN,
FEDERAL ENERGY REGULATORY COMMISSION,
Petitioners,

v.

MID-LOUISIANA GAS COMPANY, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF AMICUS CURIAE OF PUBLIC POWER GROUP IN SUPPORT OF PETITIONERS

Pursuant to the provisions of Rule 36.4, the Public Power Group [1] respectfully submits this brief amicus curiae in support of petitioners and urging reversal of the court of appeals' judgment and opinion in *Mid-Louisiana Gas Co.* v. *Federal Energy Regulatory Commission*, 664 F.2d 530.

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[1] The individual members of the Group—each of which is "a political subdivision of a State" within the meaning of Rule 36.4—are listed on the inside front cover of this brief.

INTEREST OF AMICUS CURIAE

Amicus Public Power Group consists of some seventy municipal and other publicly owned energy systems, each of which provides electric or natural gas service to its citizens. The electricity is generated in part, and the natural gas service is provided, by natural gas purchased from various pipeline companies, and the cost of the gas thus purchased forms an important element of the rates which members of the Public Power Group charge their customers. In 1981, members of the Group served more than 2,300,000 customers in fifteen States; in providing this service, they purchased in excess of 158,000,000 Mcf of natural gas.

In holding that the Federal Energy Regulatory Commission's long-recognized ratemaking jurisdiction over pipeline-produced gas under the Natural Gas Act of 1938 was impliedly repealed by the Natural Gas Policy Act of 1978, the court below mandated that gas produced by pipelines receive the substantially higher incentive price levels which the 1978 Act provides for independent producers. The effect of the decision—not addressed by the court of appeals—will be to raise gas costs substantially for customers of producing pipelines, without in any way providing the exploration incentive that the NGPA levels were designed to achieve. This windfall for the affected pipelines will be paid for by sharp and unwarranted increases in the gas costs of members of the Public Power Group, forcing them to increase the rates to their customers, or, in those cases where the unwarranted increases push the price of gas above the price of competing fuel, force an increased reliance on foreign oil, contrary to articulated national energy policy.

SUMMARY OF ARGUMENT

In holding that the Natural Gas Policy Act of 1978 repealed, by implication, the Federal Energy Regulatory Commission's long-standing authority to set prices for natural gas produced and sold in interstate commerce by natural gas pipelines, the court of appeals committed two fundamental errors. First, it erred in basing its drastic construction of the 1978 Act on an inconclusive definitional clause, in the absence of any expression in the legislative history of a Congressional intent to mandate higher prices for pipeline production.

Second, in promulgating a far-reaching and essentially legislative result—that, as a matter of law, the Commission may not fix a different price for *pipeline* production than the Congressionally fixed price for *independent producer* production—the court of appeals not only reversed the judgment of the expert agency charged with administration of the two statutes in question, but, more importantly, ignored the broader legislative considerations of the cost to the public of its interpretation and the resultant impact on overall national energy policy. While it is appropriate for a court to clarify ambiguous language in order to effectuate the clearly stated legislative design, the effect of the decision below is to produce drastic and wholly unexpected results—significantly changing long-standing regulatory law—in the absence of any evaluation by either the Congress or the Commission of the consequences of such a change.

ARGUMENT

Background

The natural gas industry is comprised of three separate functions—production, transmission, and distribution—each of which has typically (though, as this case demonstrates, not universally) been performed by a separate entity. From the early years of this century, the distribution entity had been regulated at the state level, but state agencies were constitutionally precluded from regulating the wholesale price paid by distributors to their interstate suppliers, and in 1938 Congress passed the Natural Gas Act, 52 Stat. 821, 15 U.S.C. § 717 *et seq.*, giving the Federal Power Commission jurisdiction to fix "just and reasonable rates" for natural gas sold for resale in interstate commerce. The Commission initially held that, under the Natural Gas Act, its jurisdiction was limited to transmission companies (i.e., interstate pipelines) and to the rates which pipelines charged distributors, but did not extend to producers or to the rates which producers charged pipelines. Many pipelines, however, in addition to their transmission function, also engaged in exploration and production, providing a portion of their overall gas supply from their own production while purchasing the balance from independent producers (that is, producers not affiliated with an interstate pipeline). From the beginning, the Commission exercised rate jurisdiction over a pipeline's own production, typically setting a resale rate based on the pipeline's actual cost of production (including the cost of unsuccessful exploration and a return on investment). Efforts by the pipelines to obtain "parity" with independent producers (i.e., to price their pipeline production by reference to the unregulated prices obtained by independent producers) were ultimately rejected by the courts as unlawful under the Act, see *City of Detroit* v. *F.P.C.*, 230 F.2d 810 (D.C. Cir. 1955), cert. denied, 352 U.S. 829.

In 1954, this Court held that interstate sales by independent producers were subject to Commission regula-

tion under the Natural Gas Act, *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, and the Commission embarked on the statutorily required cost-based regulation. After initially attempting to fix each producer's rates by reference to the producer's individual costs, the Commission opted for an industry-wide approach, under which producer rates approximated industry average costs, and this Court affirmed, *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968).

Responding to the pipelines' complaint that continued individual-company costing for pipeline production hampered the pipelines' ability to compete with independent producers in acquiring new gas leases, the Commission, in 1969, provided that pipelines would be given the independent-producer price for production from leases acquired after 1969, unless the pipeline requested and justified cost-of-service treatment for such production,[2] *Pipeline Production Area Rate Proceeding*, 42 FPC 738, aff'd, *City of Chicago* v. *F.P.C.*, 458 F.2d 731 (D.C. Cir. 1971), cert. denied, 405 U.S. 1074. Individual-company costing was continued, however, for production from leases acquired prior to 1969.[3]

It was against this background that Congress, in November 1978, enacted the Natural Gas Policy Act, 92 Stat. 3351, 15 U.S.C. § 3301, the statute whose interpretation has spawned the instant litigation. Like many a piece of compromise legislation—and the NGPA was, perhaps, more compromised than most[4]—the statute presents cer-

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[2] This exception would be of benefit to pipelines experiencing a higher-than-industry-average cost of production.

[3] It should be noted that this case involves only the Commission's statutory authority to continue individual-company costing on production from (1) pre-1969 leases and (2) those post-1969 leases where the pipeline had requested and received permission to use a cost-of-service approach.

[4] See, e.g., Judge Wilkey's description of the legislative history, *Consumer Energy Council* v. *F.E.R.C.*, 673 F.2d 425 at 435-36 (D.C. Cir. 1982).

tain difficulties; yet its principal features can readily be discerned. Enacted as a compromise between those who wished to overrule this Court's *Phillips* decision and deregulate independent producers altogether, and those who wished to extend regulation to the intrastate market, the NGPA replaced the prior cost-based producer rates that had been established by the Commission with a series of higher statutory ceilings, and applied the new ceilings to both intrastate and interstate production.

There is, significantly, nothing in the language of the NGPA which states that the new statutory price ceilings are to apply to pipeline production, and nothing in the legislative history bespeaks a Congressional intent to end the separate treatment for pipeline production that had existed for forty years—both pre- and post-*Phillips*. Thus, when the Commission—which had not only presided over the problems which had led to the NGPA, but had actively urged Congress to enact the new legislation—came to review the impact of the statute on its jurisdiction over pipeline production under the Natural Gas Act, it concluded, in the orders vacated by the court of appeals, that the new statute left its Natural Gas Act jurisdiction over pipeline production unimpaired.

I. The Court of Appeals Erred in Holding That NGPA Impliedly Repealed Commission Jurisdiction Over Pipeline Production.

The heart of the Natural Gas Policy Act is to be found in Title I (NGPA Sections 101-110), which establishes a series of statutory price ceilings for different categories of wellhead sales—onshore, offshore, old, interstate, intrastate, high-cost, and stripper wells. In each case, the statute provides that the ceiling should apply to the "first sale" of the gas involved. The term "first sale" is apparently a new addition to the governing statutory language: in the typical chain of sales, the first sale of natural gas is the sale by the producer to the pipeline at the

wellhead; the second sale is the sale by the pipeline to the distributor at the city gate; and the third sale is the sale by the distributor to the consumer at his home, plant, or office.

In vacating the Commission's orders here, the court of appeals relied primarily on its construction of NGPA's definitional section (NGPA Section 2, 15 U.S.C. § 3301), and in particular Subsection 21, which defines "first sale". In somewhat convoluted fashion, Subsection 21 first defines "first sale" to include *any* sale *to* a pipeline (typically the first sale), to a distributor (typically the second sale), or to a customer (typically the third sale), then cures this overbroad definition by excluding from the foregoing any sale *by* a pipeline (typically the second sale) or *by* a distributor (typically the third sale) "unless such sale is attributable to . . . gas produced by such . . . pipeline [or distributor]." [5] Because the court of appeals rested its ultimate conclusion on the need to give "meaning" to the unless clause, careful examination of both the language and the industry practice is essential.

Although pipelines which engage in exploration and production normally do so in order to acquire gas reserves for their pipeline system, they frequently discover gas located too distant from their pipeline system to be economically used within the system. Accordingly, such gas is sold to the nearest pipeline available; and such a sale is termed an "off-system" sale. Although, as noted

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[5] Read literally, the "unless" clause would appear to place into the "first sale" category the pipeline's city-gate sale to a distributor of any gas that included a portion of the pipeline's own wellhead production. Such a construction—which it may be noted, has *not* been urged by any party or by the court below—would be detrimental to the pipeline and beneficial to the consumer, for it would apply the "first sale" wellhead price (which includes no allowance for transportation costs) to the city gate sale, which is made *after* transportation. Yet such a construction is by no means frivolous: the city-gate sale to the distributor after transportation of the pipeline's production is, in fact, the first sale of such gas.

supra, the Commission had, both pre-*Phillips* (when independent producers were unregulated) and post-*Phillips* (when they were not), treated pipeline production differently from independent-producer production, it had, for many years, accorded independent-producer treatment to a pipeline's *off-system* sales, see, e.g., *Pipeline Production Area Rate Proceeding*, Opinion No. 568, 42 FPC 738 at 746 (1969). Consistent with this long-standing practice, the "unless" clause of Subsection 21 continues this parity for a pipeline's off-system sales—i.e., accords "first sale" producer pricing to a sale *by* a pipeline attributable to gas produced by such pipeline.

Hence the linchpin of the court of appeals' reasoning collapses: The court below is factually incorrect in holding that the "unless" clause of Section 2(21)(B) would be rendered "a nullity" (App. 9, 664 F.2d at 535) if it were not interpreted to include *all* pipeline production within the "first sale" definition. To the contrary, and as the Commission correctly held, without the "unless" clause, a pipeline's off-system sales would be denied "first sale" treatment, a result that would be a sharp departure from the Commission's pre-NGPA treatment of off-system sales. The complete absence of *any* legislative history on this aspect of Section 2(21) strongly suggests that the Act's draftsmen, its sponsors, the Congress, the Commission, the industry, and the public all understood that, on this point, no change in prior practice was being made. Not only was the NGPA the last in a series of efforts to obtain deregulation for independent producers—not pipeline producers—but it is beyond belief that Congress would, in light of the much-litigated question of Commission regulation of pipeline production under the Natural Gas Act, wipe out forty years of jurisdiction via an involuted definition clause and without any recognition—in the Committee Reports, in the Congressional debates, or elsewhere—that it was doing so.

The court's other supporting reasons, to the extent that they do not rely on its erroneous "need to give meaning to

the unless clause" thesis, are equally deficient. The court's comment (App. 8-9, 664 F.2d at 535) that "nothing in the language [of NGPA] . . . suggests any intent to deny NGPA pricing to natural gas just because it is produced by a pipeline" ignores the obvious, that existing law can be changed only by affirmative Congressional action, and begs the critical question whether the language of NGPA *grants* first sale pricing to pipeline production. The court's reliance on its understanding of the legislative purposes of NGPA (App. 9-10, 664 F.2d at 535-36) fares no better. While encouragement of exploration and production was *one* of the purposes of the Act, the NGPA was, as noted *supra*, the product of many compromises, and both in the debates and in the drafting of the statute the critical questions were how much encouragement was necessary and at what cost. Clearly, it is no proper function of a court of appeals, in reviewing FERC action under the NGPA, to require more encouragement, at higher cost, than Congress intended. And, in any event, granting NGPA ceilings to old pipeline production which has long been committed to interstate commerce will in no way encourage exploration and production.[6]

The court's belief that its statutory construction would further NGPA's goal of eliminating "the dual interstate and intrastate market for natural gas" (App. 9-10) is difficult to follow and appears, at best, to be based on a misapprehension of the problem Congress was addressing. The "dual market" related to the fact that *independent producers* were selling their new reserves to the intrastate market rather than to the interstate market in order to obtain higher prices; it had nothing whatever to

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[6] It is noteworthy that the court below made no effort to explain how allowing NGPA ceilings to pipeline production from pre-1969 leases would increase production. Its characterization of the Commission's argument as "sophistic" is, of course, neither an explanation nor an answer.

do with pipeline production—whether interstate or intrastate—whose regulatory treatment is at issue here.[7]

More remarkable, however, is the court of appeals' thesis that where a pipeline produces gas as part of its system supply, transmits that gas through its pipeline system, and sells the gas to a local distribution company, *two* sales take place: one (without benefit of contract, transfer of title or consideration) from the pipeline to the pipeline, and the second from the pipeline to the distributor. Although noting that the Commission had held that, under such circumstances, there was no "sale" by that pipeline to the pipeline, the court of appeals failed to address the statutory definition of "sale" provided by NGPA Section 2(20): "The term 'sale' means any sale, exchange, or other transfer for value;" or to explain how, even in the absence of a statutory definition, a "sale" can occur without transfer of title or consideration. It should, of course, be emphasized that the wellhead pricing scheme established by Title I of the NGPA sets statutory ceilings, and provides that the effective price shall be the ceiling or the contract price, whichever is lower. Since the fictitious pipeline-production "sale" created by the court of appeals involves no contract, the effective price is the ceiling, and rather than merely achieving "producer parity", the pipeline achieves *more* than "producer parity".

II. The Result Reached by the Court Below Conflicts With National Energy Policy.

In holding, in the complete absence of any significant evidence of legislative intent, that Section 2(21) of the Natural Gas Policy Act stripped the Commission of its power to fix just and reasonable rates for pipeline production, the court below made what is essentially a legis-

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[7] The court's reliance (App. 11-12) on NGPA Section 203(b)(2)—a part of Title II, dealing with incremental pricing—to support its interpretation of a Title I "first sale" is, all else aside, precluded by the language of the Section itself, which prescribes a rule solely "for purposes of this section."

lative determination—but one reached without any consideration of its economic consequences or its relationship to broader national energy policies. This failure is especially ironic here: The NGPA was one of five major energy statutes considered as a package by the House of Representatives; the principal basis on which the legislation was sold to the Congress was the need for an integrated national energy policy, and it is generally agreed that the NGPA could not have survived an up-or-down vote on its own but required the five-act National Energy Act package for passage, see, e.g., *Consumer Energy Council* v. *F.E.R.C.*, 673 F.2d 425 at 435-36 (D.C. Cir. 1982). Yet, the decision below seriously tilts the compromises worked out in the NGPA, and drastically changes one aspect of national energy policy.

Four important areas that would have been considered by the Congress (or by the Commission) had it desired to change the prior policy on pipeline production were either inadequately considered or not considered at all by the court below. These four are (1) alleged benefit to production, (2) impact on prices, (3) impact on other energy policies, particularly dependence on imported oil, and (4) impact on the economy.

1. *Alleged Benefit to Production*

While the Natural Gas Policy Act was, as suggested earlier, a bitterly contested piece of legislation whose wisdom has frequently been challenged, there can be no question that the Act struck a series of quite specific balances between allowing higher prices in order to avert energy shortages and avoiding unwarranted price increases that would be unfair to the consumer and would needlessly burden the economy. The Congress considered, and rejected, the alternative of complete decontrol; and much of the length and complexity of the Act as passed can be attributed to the Congressional decision *not* to treat all gas the same for pricing purposes, but to create a whole series of different categories, and to establish different

regulatory treatment for each of those categories. Moreover, Congress was aware that conditions would change over time, and in the NGPA, more than in most statutes, it left the agency charged with administering the statute considerable discretion to interpret and apply the statutory language, see, e.g., NGPA Section 501(a), 501(b).

Although the court below asserted that its result would promote the statutory "goal of increasing natural gas production" (App. 9, 664 F.2d at 535), it failed to explain how this would, or could, occur. The higher prices would apply to gas long since discovered—and, in fact, discovered with consumer moneys without risk to the pipeline's shareholders. The absence of a persuasive showing on this score by the pipeline claimants before either Congress or the Commission cannot be remedied by a conclusory statement of the court of appeals.

2. *Impact on Prices*

While the court of appeals' conclusory statement on encouragement of production is inadequate, the court made no effort whatever to determine or weigh the extent of the adverse impact that would result from increased prices for pipeline production. There can be no question that the increased costs would be large indeed, with estimates ranging from the hundreds of millions to in excess of one billion dollars.[8]

Any rational decision-making in the energy field—whether undertaken by the Congress or by the Commission—must obviously weigh the indicated benefit of a proposed change against the estimated cost, and there is evidence that both Congress and the Commission did so here.

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[8] It is significant that, in opposing grant of certiorari, the pipeline respondents criticized the estimates appearing in the several petitions for certiorari, but failed to supply estimates of their own. This failure is surprising, since each pipeline is obviously well aware of how large a rate increase it has claimed, or will claim, as a result of the decision below.

Yet the court below, in construing Section 2(21) by reference to its perception of *one* of the statutory goals (encouraging production) while eschewing any cost-benefit analysis, ignored countervailing, but equally important, goals.

3. *Impact on Other Energy Policies*

For a variety of reasons, the price of natural gas at the wellhead and to the consumer has risen drastically in recent years, and the additional increases mandated by the decision below may well force the price of gas above the price of competing fuels.[9] It is with this aspect of increased cost that amicus Public Power Group is particularly concerned, for the sharply higher prices resulting from the court of appeals' decision could well force a shift away from gas to imported oil, contrary to declared national energy policy.

Although the Powerplant and Industrial Fuel Use Act of 1978, P.L. 95-620, 92 Stat. 3289—enacted along with the NGPA as part of the National Energy Act—originally placed limitations on the use of natural gas to generate electricity (PIFUA, Section 301(a)), the Act gave the Department of Energy authority to grant exemptions, where found to be in the public interest, on a case-by-case basis. Pursuant to that authority, the DOE found the use of natural gas in the generation of electricity to be in the public interest and in furtherance of national energy policy, see, e.g., DOE, Economic Regulatory Administration, Public Interest Exemption Option Analysis (Feb. 21, 1980), p. A. 7 ("It is in the national interest to substitute domestic natural gas for expensive, imported oil"); DOE, Economic Regulatory Administration, Order Granting Exemptions (Mar. 4, 1980), pp. 16-17 ("It is essential that the Nation immediately reduce its reliance on imported

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[9] Recent pipeline filings with the Federal Energy Regulatory Commission indicate that, on many pipelines, the price of gas already exceeds the price of fuel oil.

oil. . . . Expanded use of natural gas [to generate electricity] would be a significant step . . . to reduce [U.S.] demand for imported oil"). In 1981, the Congress, giving explicit recognition to the type of policy considerations relied on by DOE in its Public Interest Exemption Orders, repealed Section 301(a) of PIFUA, Omnibus Budget Reconcilation Act of 1981, § 1021(a), P.L. 97-35, 95 Stat. 614, and see House Budget Committee Report, H. Rept. 97-158, Vol. II, pp. 6-8.

Thus, at the very time that Congress, as part of an overall national energy policy, is seeking to substitute domestic natural gas for imported oil, the decision of the court below, by needlessly raising gas prices above the price of oil, discourages the use of natural gas and promotes increased use of foreign oil.

4. *Impact on the Economy*

In modifying the fabric of economic regulation of natural gas at a time when the failing state of the economy is the nation's prime concern, the court of appeals ignored the impact of its decision on the overall economy. As discussed *supra*, higher prices for pipeline production previously priced on a cost-of-service basis cannot encourage production, and, in any event, higher production rates are unnecessary in this period of excess supply. Yet the increased costs—a pure unearned windfall to the pipelines—will either cause loss of sales, with an idling of industrial capacity, or a diversion to imported oil, or will drain dollars from the consumer, whose hoped-for increased spending, particularly on durables, is relied on to lead the economy out of its present deep recession.

There is now general agreement that the sharp increases in the cost of energy over the past decade have been a prime factor in both the rampant inflation of the 70's and the deep recession of the 80's. Totally unwarranted, judicially mandated increases, such as that required by the court below, serve merely to prolong the

present economic situation, and run counter to the nation's economic goals.

CONCLUSION

For the foregoing reasons, the Public Power Group respectfully requests that the judgment of the court of appeals be vacated, and that the case be remanded with directions to affirm the orders of the Federal Energy Regulatory Commission.

Respectfully submitted,

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Docket Sheet

NO. 81-1889-CFX Vide: 81-1958, 81-2042 See: 81-1672	TITLE	Public Service Commission of the State of New York, Petitioner v. Mid-Louisiana Gas Company, et al.

DOCKETED	COURT
Apr. 12, 1982	United States Court of Appeals for the Fifth Circuit

DATE	PROCEEDINGS AND ORDERS
	Counsel for Petitioner: Richard A. Solomon
	Counsel for Respondents: Solicitor General, Philip J. Mause, James D. McKinney, Jr., Kim M. Clark, Raymond N. Shibley, Philip C. Wrangle, Frank X. Kelly (Over)
Apr. 12, 1982	Petition for writ of certiorari filed. (Record filed).
Apr. 12, 1982	Appendix filed.
May 10, 1982	Motion of Public Utilities Commission of the State of California, et al. for leave to file a brief as amici curiae filed. (Vide: 81-1958, 81-2042).
May 11, 1982	Motion of Associated Gas Distributors for leave to file a brief as amicus curiae filed.
May 12, 1982	Brief, amicus curiae, of The State of West Virginia in support of petition filed.
May 12, 1982	Motion of the State of Kansas, et al. for leave to file a brief as amici curiae filed.
May 11, 1982	Order extending time for respondent Mid-Louisiana Gas Company, et al. to file a response to the petition until June 15, 1982.
May 13, 1982	Brief, amici curiae on behalf of The Commonwealth Of Pennsylvania and The Pennsylvania Public Utility Commission in support of petitioner filed. (Vide: 81-1958)
May 20, 1982	Opposition to motion of Public Utilities Commission of the State of California, et al. for leave to file a brief as amici curiae filed by Colorado Interstate Gas Co. (Vide: 81-1958, 81-2042).
May 20, 1982	Order extending time for respondent El Paso Natural Gas Company to file a response to the petition until June 15, 1982.
May 24, 1982	Response in opposition and objection of Colorado Interstate Gas Company to motions of the Associated Gas Distributors and the State of Kansas and The Kansas Corporation Commission for leave to file briefs as amicus curiae filed.
May 25, 1982	Brief of respondent Colorado Interstate Gas Company in opposition filed. (Vide: 81-1958, 81-2042).
May 26, 1982	Order extending time for the Government to file a response to the petition until July 6, 1982.
June 4, 1982	Order extending time for respondents "Pipelines" to file a response to the petition until July 15, 1982.
	(Over)

81-1889

Title

No.

DATE	PROCEEDINGS AND ORDERS
	Counsel for respondents' cont'd: George W. McHenry, Jr. John E. Holtzinger, Jr., William Michael Lange
June 28, 1982	Brief, amicus curiae, of Public Power Group in support of petition filed. (Vide: 81-1958, 81-2042).
Aug. 4, 1982	Brief in opposition of respondents Kansas-Nebraska Natural Gas Company, Inc., et al. filed. (Vide: 81-1958, 81-2042, 82-19).
Aug. 4, 1982	Brief of respondent Kentucky West Virginia Gas Company in opposition filed. (Vide: 81-1958, 81-2042, 82-19).
Aug. 4, 1982	Brief of respondent Consolidated Gas Supply Corporation in opposition filed. (Vide in all cases).
Aug. 4, 1982	Brief of respondent Kansas-Nebraska Natural Gas Company, Inc. in opposition to Brief amici curiae State of Kansas and Kansas Corporation Commission filed.
Aug. 4, 1982	Motion of the National Rural Electric Cooperative Association for leave to file a brief as amicus curiae filed. (Vide in all cases).
Aug. 5, 1982	Brief of El Paso Natural Gas Company in opposition filed. (Vide in all cases).
Aug. 5, 1982	Brief of respondent Mid Louisiana Gas Company in opposition filed. (Vide in all cases).
Aug. 5, 1982	Motion of Edmund G. Brown, Jr., Governor of California for leave to file a brief as amicus curiae filed. (Vide in all cases)
Aug. 11, 1982	DISTRIBUTED. SL17P1.
Aug. 16, 1982	Response in opposition and objection of Colorado Interstate Gas Company to motion of Edmund G. Brown, Jr., Gov. of California, for leave to file brief amicus curiae filed. (Vide in all cases)
Aug. 19, 1982	Opposition of respondent Colorado Interstate Gas Company filed.
Aug. 25, 1982	Opposition of respondent Consolidated Gas Supply Corporation to motions for leave to file briefs amicus curiae filed. (Vide: 81-1958, 81-2042, 82-19).
Sept. 20, 1982	Reply brief for the petitioner filed. (D).
Oct. 4, 1982	The motion of Public Utilities Commission of the State of California et al. for leave to file a brief as amici curiae in Nos. 81-1889 81-1958, 81-2042 is GRANTED. The motion of Associated Gas Distributors for leave to file a brief as amicus curiae in No. 81-1889 is GRANTED. The motion of National Rural Electric Cooperative Association for leave to file a brief as amicus curiae is GRANTED. The motion of Edmund G. Brown, Governor of California, leave to file a brief as amicus curiae is GRANTED . Petition GRANTED
The Case	is consolidated with 81-1959, 81-2042 and 82-19 and a total of one hour is allotted for oral argument.

(Card No. 2)

NO. 81-1889-CFX	TITLE Public Service Commission of the State of New York, Petitioner v. Mid-Louisiana Gas Company, et al.

DOCKETED	COURT
Apr. 12, 1982	United States Court of Appeals for the Fifth Circuit

DATE	PROCEEDINGS AND ORDERS
Nov. 9, 1982	Motion of parties to dispense with printing the joint appendix filed. (Also in 81-1958, 81-2042, 82-19).
Nov. 18, 1982	Motion of the Public Utilities Commission of the State of California, et al. for leave to file a brief as amici curiae in support of petitioners filed. (Vide: 81-1958, 81-2042, 82-19).
Nov. 19, 1982	Motion of Edmund G. Brown, Jr., Governor of California, for leave to file a brief as amicus curiae filed. (Vide: 81-1958, 81-2042, 82-19).
Nov. 19, 1982	Brief, amicus curiae, of Public Power Group in support of petitioners filed. (Vide: 81-1958, 81-2042, 82-19).
Nov. 18, 1982	DISTRIBUTED. 11-24. (Motion to dispense with printing joint appendix).
Nov. 19, 1982	Order extending time to file the PETITIONER'S brief on the merits until Nov. 29, 1982, and RESPONDENTS' brief on the merits until Jan. 11, 1983.
Nov. 29, 1982	The motion of the parties to dispense with printing the joint appendix is GRANTED. The motion of Public Utilities Commission of California, et al. for leave to file a brief as amici curiae is GRANTED.
Nov. 29, 1982	Brief for petitioner The Public Service Commission of the State of New York filed.
Nov. 29, 1982	Brief for petitioner Arizona Electric Power Coorperative, Inc. filed. (Vide: 81-1958, 81-2042, 82-19).
Nov. 30, 1982	Brief for The Federal Energy Regulatory Commission filed. (Vide: 81-1958, 81-2042, 82-19).
Dec. 6, 1982	The motion of Edmund G. Brown, Jr., Governor of California, for leave to file a brief as amicus curiae is GRANTED.
Dec. 13, 1982	Motion of AZ Elec. Power Cooperative, Inc., No. 81-1958, for division of oral argument filed.
Dec. 13, 1982	Motion of petitioner in No. 81-1889 for divided argument filed.
Dec. 27, 1982	Opposition of petitioner Michigan to above two motions filed. (Only in 81-2042).
Jan. 10, 1983	The motion of Public Service Commission of New York for divided argument is DENIED. The motion of Arizona Electric Power Cooperative, Inc. for divided argument is DENIED.
Jan. 10, 1983	Brief for respondent Consolidated Gas Supply Corporation filed. (Vide: 81-1958, 81-2042, 82-19).

(Over)

81-1889

Title

No.

DATE	PROCEEDINGS AND ORDERS
Jan. 11, 1983	Brief of respondent Michigan Wisconsin Pipe Line Company filed. (Vide: 81-1958, 81-2042, 82-19).
Jan. 11, 1983	Brief of respondent Mid-Louisiana Gas Company, et al., filed. (In all vide cases).
Jan. 25, 1983	CIRCULATED.
March 11, 1983	Reply brief of petitioner Arizona Electric Power Cooperative, Inc. filed. (D). (In all vide cases).
March 14, 1983	Reply brief of petitioner The Public Service Commission of the State of New York filed. (D). In all vide cases).
March 15, 1983	Reply brief for the Federal Energy Regulatory Commission filed. (D). (In all vide cases).
March 22, 1983	ARGUED.
March 28, 1983	Motion of Public Service Commission of the State of New York for leave to file a supplemental brief after argument filed. (In all vide cases).
March 30, 1983	DISTRIBUTED. 4-1. (Above motion).
April 4, 1983	The motion of Public Service Commission of New York for leave to file a supplemental brief after argument is GRANTED.
Apr. 11, 1983	Motion of respondents for leave to file a reply to the Supplemental Memorandum of petitioners after argument filed. (In all vide cases).